Hughes Investment Advisory Service LLC

October 1, 2024

Dear Clients and Investors,

The US stock market performed well during Q3 with the S&P 500 up 5.5% and is now up 21% year to date.

Key 2024 economic data points:

- 2024 Q3 Atlanta Fed Estimated Real GDP growth: 2.5%
- 2024 Latest CPI Inflation: +2.5%
- 2024 S&P 500 YRI Estimated S&P Earnings: $250

The above numbers continue to show an economy with moderate growth, an improving inflation picture, and strong earnings growth. As I expected, US corporations with the ability to pass on higher costs have been an excellent place to be invested during this 3-year period of strong growth and high inflation.

The Federal Reserve has pivoted on the interest-rate front! The FOMC reduced the federal funds rate by half a point to 4.75%-5.0% at their most recent monetary policy meeting. This decision was prompted by an improving inflation outlook and concerns about a weakening labor market. The Fed is trying to orchestrate a so called “soft landing” for the US economy which means lowering interest rates to head off a potential recession.

As has been the case all year, economic indicators are showing a very mixed picture of the nation’s economic health. On the plus side the US consumer sector is proving resilient with consumer sentiment still strong with the Univ. of Michigan Consumer Sentiment Index rising to 69 in September however at the same time US credit card debt hit a new record, $1.14 trillion! Gold continues to hit new all-time highs which is no doubt due to lingering inflation concerns and the growing US Debt. This debt problem is clearly unsustainable and needs immediate addressing by Washington however the topic is barely discussed on the Presidential campaigns of both candidates.

So where do we stand as we head into the final quarter of 2024? The widening Middle East war remains my number one risk factor. Number two and three are similar with the Ukraine war and friction in and around Taiwan and the South China Sea. Four is the possibility of a recession. We now have a significant Port strike on the Eastern Seaboard and a massive cleanup from Hurricane Helene. History tells us that the US economy will probably plow through all this with barely a hiccup however they all deserve close

attention as we head into the Fall/Winter and a closely contested Presidential election. Remarkably the path of least resistance may continue to be higher stock prices as we head into the final quarter. How can this be with all the issues mentioned above?

Strong corporate earnings, lower inflation, strong investment inflows from overseas and now a Federal Reserve that has reversed course and started lowering interest rates for the first time in almost 5 years. When you add the overseas investment, lower interest rates and continued strong government spending it adds up to a strong tailwind for economic growth.

One theme that I have been writing about for the last 5 years is the US Governments accumulated deficit which now stands at 37 trillion up from 11 trillion in 2011. The interest on this debt is now over 1 trillion a year, surpassing the military budget in 2024. I have often warned and asked how this level of debt can be reconciled as it's clearly unsustainable in the medium to long term. What's occurred because of this debt runup is starting to become clearer with multiple downgrades to the US debt and a significant overall increase in yields on all US debt maturities. What else has resulted from this debt explosion? Strong GDP growth and corporate earnings resulting in higher equities, gold, silver, and bitcoin prices.

SO, WHAT'S HAPPENING HERE? It's slowly but surely becoming clearer to me that either intentionally or unintentionally the idea of deliberately inflating our way out of debt has been reintroduced into mainstream conversation. The term "inflating out of debt" refers to a situation where a government or an economy deliberately pursues a policy of generating inflation to reduce the burden of its debt. In this scenario the government uses inflation as a tool to decrease the real value of its outstanding debt over time. Of course, inflation also decreases the buying power of the dollar, and people's savings.

It's important to note that "inflating out of debt" can have both positive and negative consequences. On the positive side, it can provide temporary relief to governments with high debt burdens. However, it also carries risks, such as the potential for hyperinflation or loss of confidence in the currency. There is no stated policy that this strategy is being employed by the US government in fact the Federal Reserve states that interest rate policy is focused on reducing inflation to their 2% target.

The bottom line is that what the Federal Reserve says and what Washington politicians do is sometimes in conflict and therefore its critical to follow the facts and watch what's happening and not just what's being said to determine how this unsustainable debt problem will come to resolution in the years ahead. How this plays out is already affecting investment classes across the board and will be critically important in determining where we want our investment dollars invested in the future.

What else gets me excited about the US economy and markets looking into the final quarter of 2024 and beyond? Many are areas that I have discussed in previous market letters: A nuclear power renaissance supplemented by oil, natural gas, wind, and solar. A re-building of the US power grid will be needed along with these energy growth efforts which should spur the entire energy industry. The Utility industry will benefit from increased energy demand and infrastructure buildout. Industrial re-shoring. Space, aviation, and the defense sector all look primed for innovation and growth. Pharma and Med Tech should have renewed growth and interest as AI is integrated into their operations. Some of our pharma stocks have been huge winners already thanks to drug discoveries in cancer, weight loss, Alzheimer's, and soon hopefully non-opioid pain relief. Gold as an inflation hedge.

Overall, I continue to favor large-cap, dividend paying, mostly US based multi-national companies with strong balance sheets. We love businesses with irreplaceable brand names, wide moats, high margins, grow their dividends, and have modest debt. Risk/reward now seems equal between equities and fixed income – the 60/40 portfolio now works! Focused REIT's, MLP's and specialized bond/income funds look good as income producers once again. I believe that our portfolios are well positioned to produce consistently attractive long-term risk adjusted returns while preserving capital. Given all the above, I will remain vigilant, assume little, and continue to follow the investing tenants that we know, through experience, work in the medium to long-term.

Please do not hesitate to give me a call to discuss the above analysis.

Sincerely,

J. Britt Hughes
Investment Advisor Representative
Bay Colony Advisors
203.209.4797
britthughes@hiasllc.com
www.hiasllc.com

Investment advisory services offered by Bay Colony Advisors, a registered investment advisor, doing business as Hughes Investment Advisory Services LLC. No Advice may be rendered by Bay Colony Advisors d/b/a Hughes Investment Advisory Services LLC unless a client service agreement is in place. Bay Colony Advisors does not provide accounting, tax, or legal advice. No part of this newsletter should be considered investment advice. If your financial circumstances have changed, you should contact your investment advisor representative. Principal Office: 86 Baker Avenue Extension, Suite 310, Concord, MA 01742. Phone: 978-369-7200.