JOHNSON
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Quarterly Insight

MARKET UPDATE

FROM THE DESK OF CIO CHARLES RINEHART, CFA, CAIA

2024
THIRD
QUARTER

You can write just about any story you want about the third quarter. Looking only at the endpoints, it might appear to be a continuation of the bull market that began in early 2023. The S&P 500 rose 5.9%, and bond returns accelerated, with the Barclays Aggregate Index up 5.2%. Yet, for those who lived through the quarter, these summary figures don't capture the whole picture. Volatility returned to equity markets: the S&P 500 was up 4%, then down 8%, up 9%, down 4%, and up 7% again. The Federal Reserve's delicate balancing act between inflation and unemployment hit an inflection point. We witnessed rising political tensions both at home and abroad. In short, while we ended with a positive market, the quarter's summary statistics fail to tell the full story.

At the beginning of the third quarter, the market narrative remained much the same as it had since early 2023. The Federal Reserve's fight against inflation had pushed monetary policy to its most restrictive level since the Great Financial Crisis. Central bankers made it clear that inflation was still their primary concern. Meanwhile, investors reacted to the uncertainty of tighter policy by flocking to the largest U.S. companies, driven by enthusiasm over the potential of Artificial Intelligence (AI) to fuel growth, even amidst economic challenges.

July's CPI report disrupted the market's status quo. A 0.2% month-over-month increase (2.9% year-over-year) marked the lowest inflation reading since March 2021. But in economics, there's no such thing as a free lunch. Shortly after July's inflation report, new data emerged, suggesting that even easier monetary policy might not prevent a recession. July's unemployment rate rose to 4.3%, a 0.2% increase, leading some economists to warn that a near-term recession was more likely.

This set off a cascade of reactions in financial markets. Short-term interest rates began to decline meaningfully as markets anticipated potential rate cuts. Mega-cap tech stocks started to under perform, while smaller companies saw increased investor demand, as investors hoped that lower interest rates might boost their balance sheets and income statements.

At Jackson Hole, Federal Reserve Chairman Jerome Powell reviewed the post-pandemic inflation landscape, acknowledging the growing weakness in the labor market. He hinted at easier policy to come and followed through with a 0.50% rate cut in September. By the end of the quarter, labor statistics had improved slightly, giving some hope that a "soft landing" might still be possible.

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TOTAL RETURNS

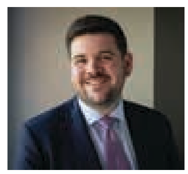
	3Q 2024	2024
S&P 500	5.9%	22.1%
Dow Jones Industrial Average	8.7%	13.9%
NASDAQ	2.8%	21.8%
Russell 2000	9.3%	11.2%
MSCI EAFE (International)	7.3%	13.0%
Bloomberg U.S. Aggregate Bond Index	5.2%	4.5%

All of this occurred against a backdrop of a looming election and escalating tensions in the Middle East; not to mention the labor strikes, assassination attempts, and a major hurricane. It would take a book to cover it all. However, focusing on key investment updates, here are our main takeaways:

> Because the economy is at a tipping point, growth could swing either way. We can expect the market to react more sharply than usual to incremental economic data until a new trend is established.

1. **Economic Transition:** We are in a transition period for the economy, with the Federal Reserve's focus shifting from inflation to unemployment. This shift is warranted based on the data. Because the economy is at a tipping point, growth could swing either way. We can expect the market to react more sharply than usual to incremental economic data until a new trend is established. While monetary policy has become more accommodative, the yield curve remains inverted, and leading indicators are still negative. The race is on to see if policy changes can take effect before unemployment worsens.
2. **Changing Market Leadership:** The shift in market leadership is significant. After 18 months of dominance by tech and AI stocks, sectors like utilities, real estate, industrials, and financials led the market in Q3. Small-cap companies outperformed large-caps, and the average stock in the S&P 500 outpaced the index itself. Bonds surged as the yield curve began to normalize. Whether this shift is temporary or long-lasting, it serves as a reminder that leadership changes over time, and yesterday's winners won't lead forever.
3. **Political Noise and Market Impact:** Expect headline noise to continue. In this political season, there is no shortage of issues for investors to worry about. We recently published a brief history of elections and their impact on markets, available on our blog. The key takeaway is that businesses have an impressive track record of adapting to the political landscape, regardless of who is in power. Politics and policy matter, but we are confident that businesses will continue to innovate and drive long-term returns in any outcome.

As always, our team is committed to staying on top of the shifting landscape and building portfolios that can adapt to the changing environment—whatever it may be. We'll return with a year-end recap and a fresh outlook in January. Until then, we thank you for your continued trust and confidence and wish you a peaceful and prosperous fourth quarter.



Chief Investment Officer, Charles Rinehart, CFA, CAIA, leads our dedicated team of research analysts and portfolio managers as they manage our investment strategies to deliver financial peace of mind to our clients.

Disclaimer: Johnson Investment Counsel cannot promise future results. Any performance expectations presented here should not be taken as any guarantee or other assurance as to future results. Our opinions are a reflection of our best judgment at the time this interview occurred, and we disclaim any obligation to update or alter forward-looking statements as a result of new information, future events or otherwise.

SCHEDULED CHANGES TO THE ESTATE TAX LAW

In 2017, Congress passed the Tax Cuts and Jobs Act ("TCJA"), which more than doubled the amount that a person can pass at death without incurring any estate tax, and that amount is indexed for inflation. But at the end of 2025, significant changes are scheduled to occur.

As a bit of background, everything that a person owns is included in their taxable estate, but there is a certain amount that can pass free of federal estate tax, often referred to as the "exclusion amount." Anything in excess of that exclusion amount will be taxed at a rate of 40%. Currently, the amount that each person can pass at their death without incurring any estate tax is $13.61 million. For a married couple, over $27 million can be passed to their beneficiaries free of estate tax. (On the death of the first spouse, there is typically an unlimited marital deduction, which defers the payment of any

SCHEDULED CHANGES TO THE ESTATE TAX LAW

estate tax that might be due to the death of the second spouse to die).

The TCJA was written in such a way that those increased exclusion amounts would go back down to the amounts in place before the law was passed (indexed for inflation). Consequently, in 2026, the exclusion amount is set to revert to approximately $7 million per person. (A married couple would have a total of approximately $14 million in exclusion available to them.)

Many of our clients are taking advantage of the federal gift tax law that is unified with the estate tax law. The exclusion amounts mentioned above are actually not just available at death, but can be utilized during life under the federal gift tax laws. So, what the combined estate and gift tax laws provide is that a person can currently pass $13.61 million at death or during their life without incurring either transfer tax. Because of this, some people are implementing planning now that takes advantage of the elevated exclusion amounts scheduled to be cut in half. For example, a married couple might establish a trust that gives one spouse lifetime access to a trust that can also benefit those who would have received the money at their death anyway. This moves assets out of their estate, as well as the growth of those assets, and allows them to take full advantage of the exclusion amount currently available. If the exclusion amount at their death is $7 million, then they no longer have any exclusion available to them at that time, but they would have moved twice that amount, plus any growth, out of their taxable estate. There are many other options for planning that can be considered in order to take advantage of the current exclusion amount.

Opinions differ as to whether the law will be changed before this scheduled adjustment. On the one hand, if the exclusion amount does go down, it will be the first time in the history of the estate tax that such a decrease would occur. (In 2010, there was a scheduled sunset of the estate tax entirely, but the law was changed that year that allowed some to opt out of the estate tax or to opt in. That was an unusual year that is unlikely to happen again.) On the other hand, if Congress does not pass new legislation, then the change happens according to the law.

Given that the law is set and that it is unclear what would happen regardless of who controls the administration or the Congress, prudence may dictate that you want to adjust your estate planning to take advantage of the increased exclusion amounts in 2025. Considering the great number of people implementing planning strategies in anticipation of the scheduled change, we strongly recommend that you contact your attorney if you wish to take advantage of the law as it currently stands. If you'd like to discuss these changes and whether planning needs to be done before 2026, we strongly encourage you to contact your portfolio manager.

IMPORTANT UPDATE

CORPORATE TRANSPARENCY ACT

We want to alert you to a new law that may impact our clients who are owners of various types of business entities. In 2021, the Corporate Transparency Act ("CTA") was enacted. The CTA created new requirements for certain entities to report to the Financial Crimes Enforcement Network ("FinCEN") starting on January 1, 2024. Scan the QR code to learn more.

NEW DESIGNATIONS

Johnson Investment Counsel is committed to continuing education to provide personal development for our employees and better service to our clients. Congratulations to Portfolio Manager Joseph P. White, CFA, CFP®, CDFA® on earning his Certified Divorce Finance Analyst® designation and to Gift Fund & Operations Associate Logan Wiedmann, CAP® earning his Chartered Advisor in Philanthropy® designation.


White


Wiedmann

NEW ADDITIONS TO THE TEAM

We are pleased to announce that these individuals have joined our team over the last several months:

- **Justin Hauser | Cincinnati**
  Equity Research Associate
- **Sarah Horrigan | Cleveland**
  Regulatory Officer
- **Jeremy Meanwell | Cincinnati**
  Equity Research Associate
- **Joanna Pereira | Cincinnati**
  Front Desk Associate


Hauser


Horrigan


Meanwell


Pereira

IN THE NEWS

The expertise of our Johnson team members is often sought after by local and national media sources. Scan the QR code to see recent articles and videos featuring our employees.

UPCOMING WEBINARS

Are you a current or former Procter & Gamble employee? This webinar, led by Michael Stanis, CFA, CFP®, MBA, a former P&G employee, is designed to help owners of the P&G Profit Sharing Trust (PST) understand how the proceeds may be distributed and invested, and how taxes are impacted. Johnson Investment Counsel has helped hundreds of P&G employees navigate PST distribution options. We want to share what we know so that you can make the best decisions for your family.

SCAN TO REGISTER

Are you maximizing your retirement plan benefits? Learn about the Mega Backdoor Roth strategy to potentially unlock up to $69,000 in tax-free savings. Join Portfolio Manager Christian Brandetsas, CFP®, for a free 30-minute webinar to discover how this strategy can enhance your long-term financial security.

SCAN TO REGISTER

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ABOUT US

Johnson Investment Counsel is one of the nation's largest independent wealth management firms, managing more than $20 billion in assets for clients in 50 states. Johnson Investment Counsel is an employee-owned firm, offering a full range of fee-only, integrated wealth management services, including: investment portfolios, education and retirement planning, cash management, estate planning, trust services, charitable giving, mutual funds, 401(k) plans, IRAs, and more. Johnson Investment Counsel has built strong, long-term relationships with individuals, families, charitable organizations, foundations, and corporations through four integrated divisions.

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