Advyzon
INVESTMENT MANAGEMENT

Panoramic Market View

Review and Outlook | January 2025

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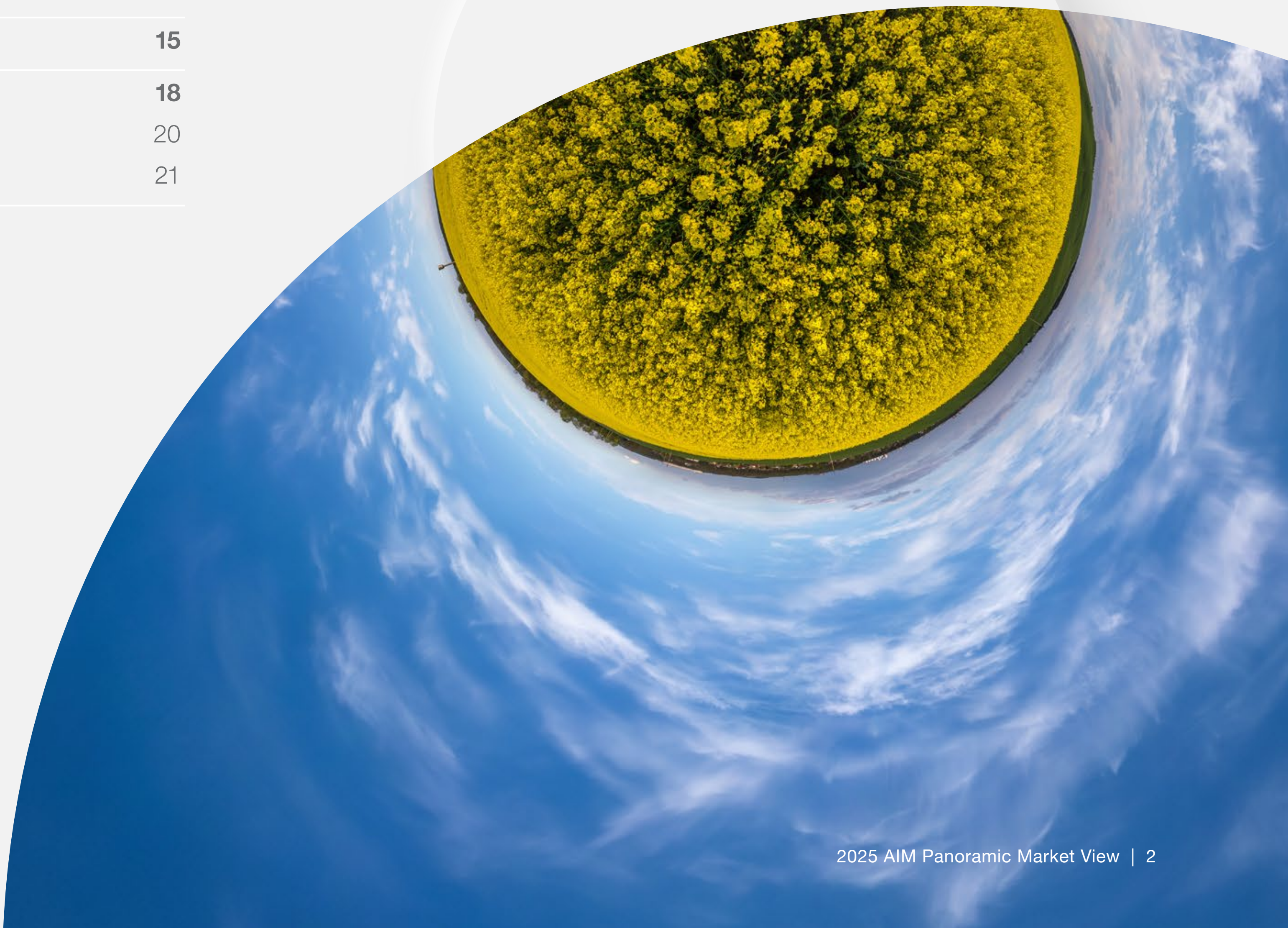


From the CIO

2024 was a good year for investors in nearly all asset classes following a terrific 2023. US equity markets enjoyed above average returns while the majority of international stock markets had below average, but positive results. Bond prices dropped for most fixed coupon bond maturity ranges, but healthy coupon payments kept total returns in the black for all but the longest maturity bonds.

Market fluctuations for the year were driven a great degree by three broad topics; political success by Republicans, continuing fervor for artificial intelligence related investments, and Fed rate cuts. In 2024, there were seven days when the S&P 500 was up more than 1.5% and nine days when the S&P 500 was down more than 1.5%. When we look back at headlines for every one of these days with outsized market movements, the lead story is related to one of these three topics—some days for the positive and some days for the negative.

For the first time in 130 years, we have a new/repeat president taking office in January, one that has a history of making bold changes with large ramifications for financial markets. Republicans in general and Trump specifically have a reputation for being "friendly" to economic markets. This explains why November 6, the first business day after the election, was the largest up day for the year for the S&P 500 index, with a jump of 2.5%.

Stock prices grew significantly in 2024 in part on earnings growth, but also on valuation expansion. Earnings grew from $192 per share of the S&P 500 index in 2023 to $208 per share in 2024, an increase of 8.3%. This growth is in line with the average earnings growth of 8.1% we saw between 1960 and 2023. The price level of the S&P 500 index grew from 4,770 to 5,882 during 2024, an increase of 23.3%, so we can infer that the valuation expansion was 15.0%. We agree with Warren Buffet's famous quote that interest rates are the most important factor in stock valuation, and the Fed did drop rates by 1.0% in 2024 and we may see additional cuts in 2025, but the 15.0% valuation expansion seems a bit overdone. Even if many hoped-for artificial intelligence related innovations become cash flow positive during the next few years, it may take many years to "grow into" the S&P 500's year ending price-to-earnings multiple of 27.1.

After two strong years of performance for large US stocks, investors have become increasingly skittish, worried that the likelihood of a pullback has increased. Our analysis agrees with this

Brian Huckstep, CFA, CFP®
Chief Investment Officer

concern, however, history is on the side of remaining in stock markets. Since 1926, large US stocks have had 11 occurrences (not counting 2023/2024) where annual returns for the S&P 500 index exceeded 20% for two consecutive years. The average return in year 3 for those 11 occurrences was 6.7%, a return that is below the long run average return of 12.3%, but above the current yield on most bonds and on cash.

The yield curve reverted back to a normal, upward slope in mid-December, after two years of being inverted (where shorter-term bonds paid more than riskier longer-term bonds). This led to negative performance for longer-term bonds in 2024, but has left yields much more attractive than they have been for many years, warranting consideration in portfolios that allocate to bonds.

While in many ways 2024 gave us a repeat of 2023 for the securities markets, we do not expect more of the same for 2025. We look forward to providing you a panoramic view in 2025—one that captures the full scope and depth required to navigate the evolving landscape and seize the potential that lies ahead.

Brian Huckstep, CFA, CFP®
Chief Investment Officer

Report Contributors

Brian Huckstep, CFA, CFP®
Chief Investment Officer

Alex Riedel
Managing Director
Head of Client Portfolio Management

Carolyn Szaflyk
Senior Client Portfolio Manager

Mike Gray
Trader

Dominic Golminas
Trader

Macroeconomic Review

Security prices are impacted significantly by changes in Gross Domestic Product (GDP). As goes GDP, so go corporate profits and stock prices. The new incoming federal administration has exciting ideas for changes to many policies and it is an interesting time for macroeconomists who forecast the impact of changes. One framework to help us forecast potential impacts for securities markets is the formula for the GDP expenditure approach—

GDP = Consumer Spending + Government Spending + Investment + (Exports minus Imports)

By understanding the potential impact of proposed changes on each component of GDP, we can formulate an expectation for the net impact of the most important changes.

Reasons GDP may decrease

1. Decreased federal spending (Straightforward reduction of Government Spending)
2. Deportations (Less people living and spending in the US consuming (legal or illegal) means less Consumer Spending)
3. Fizzling of AI investing (AI spending has been high with little increase in corporate profits so far—Investment could drop)

Reasons GDP may increase

1. Tariffs (Increased prices for imported goods decrease demand and prompt US consumers to buy US products—reducing Imports)
2. Lower Taxes (When consumers are paying less tax, Consumer Spending can increase)

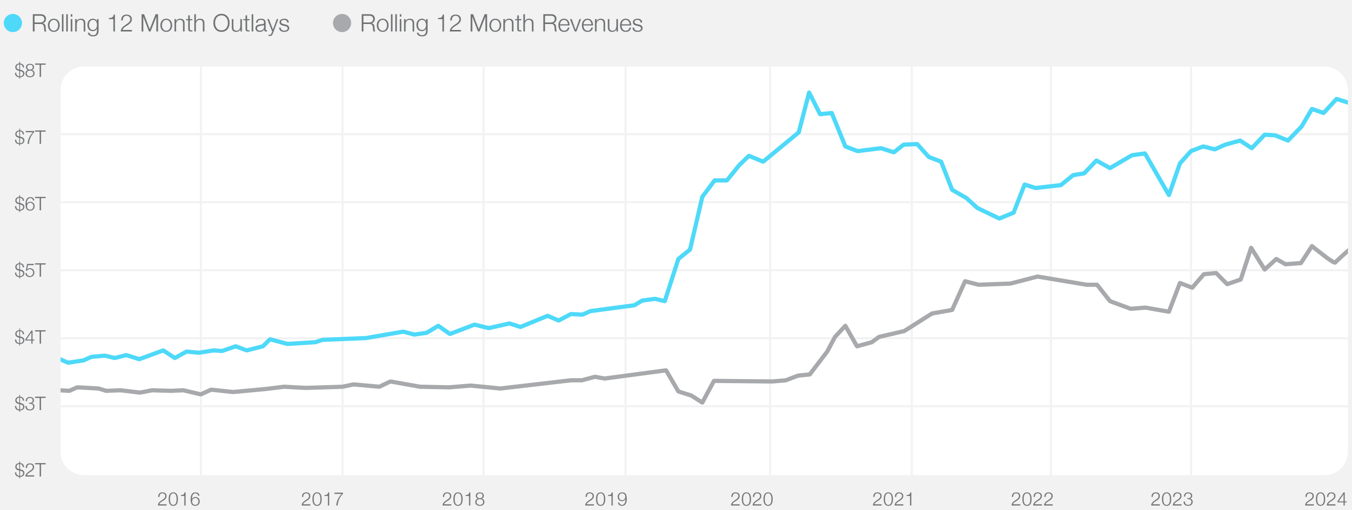
Many expert groups have written research that estimate the potential size impact of each of these factors, but on the whole, these changes are most likely to add up to a net headwind for GDP in 2025. It is important to note that there are many non-GDP related reasons to enact these changes, such as; reducing the federal deficit, reducing crime, and increasing good job opportunities for working Americans—so we are not suggesting these changes should not be done. The size of the potential impact to GDP during the next few years will depend on the speed at which these changes are implemented. We expect most of these changes will happen gradually enough that natural GDP growth (including inflation) will overcome growth drag from these changes, but we worry that the market may have difficulty hitting the long run average Earnings Per Share growth of 8.1% in 2025, let alone the 14.8% earnings growth rate that FactSet is reporting analysts have baked into their forward expectations and discounted cash flow models.

The ever-growing US national debt is a risk that warrants attention by investors. In early 2011, Bill Gross, who was then known as the "Bond King" from PIMCO, wrote and spoke about his concerns of a US debt default because of the growing budget deficit and rising debt. He went so far as to short treasury bonds in his portfolios. US Federal debt was $15 trillion back then and has more than doubled to $36 trillion today. Mr. Gross was clearly quite early with his portfolio tilt, as the US Department of Treasury has continued to pay the interest and principal due on the bonds. However, his concerns are valid—our politicians have been borrowing copiously today against tomorrow.

The chart below shows a 10-year history of rolling revenues and spending for our federal government. There is clearly a problem with runaway spending, but the spending gap could also be helped with additional taxation (including taxes from tariffs).

The most important risk that the high level of US debt imposes on investors is that issuance may so greatly exceed bond demand, that the US Treasury has to drop the price of the debt by a meaningful

U.S. Federal Spending vs Taxes—Rolling 12-Month Data—2015 through 2024



Source: https://fiscaldata.treasury.gov/ Monthly Treasury Statements (MTS) percent to get all of the bonds to sell at its auctions. That kind of price drop carries over to existing debt of similar bonds with similar maturity and would generate losses for existing holders of US government debt. It is not just the new annual deficit that must be financed with bond sales, but historical debt must also be rolled over as it matures. It is impossible to know when the day that the US Federal Debt Tipping Point will come (I am coining that term here today), but demand for treasury bonds is not infinite and that event is getting closer every day. Although Trump's pledges of spending cuts and tariffs will help push the annual deficit in the right direction, his promise of lower taxes mixed with his history of running up the debt during his first term, leads us to recommend cutting back on US treasury bond exposure in favor of credit bonds and mortgage backed bonds. Credit bonds and mortgage backed bonds have also seen increases in issuance, but not at the same extreme growth rate as the US government's debt.

International markets would clearly be impacted negatively by US tariffs that reduce demand for their goods. Prices for international stocks were already impacted significantly in Q4 2024, as Trump's tariff rhetoric became more vitriolic, so the relative impact on non-US stock prices in 2025 may be muted.

Asset Class	**Index Name**	**Oct 2024 Return**	**Nov 2024 Return**	**Dec 2024 Return**	**Total Return 4th Qtr. 2024**
US Stocks	S&P 500	-0.9	5.9	-2.4	2.4
International Developed Stocks	MSCI EAFE NR	-5.4	-0.6	-2.3	-8.1
Emerging Markets Stocks	MSCI EM NR	-4.4	-3.6	-0.1	-8.0

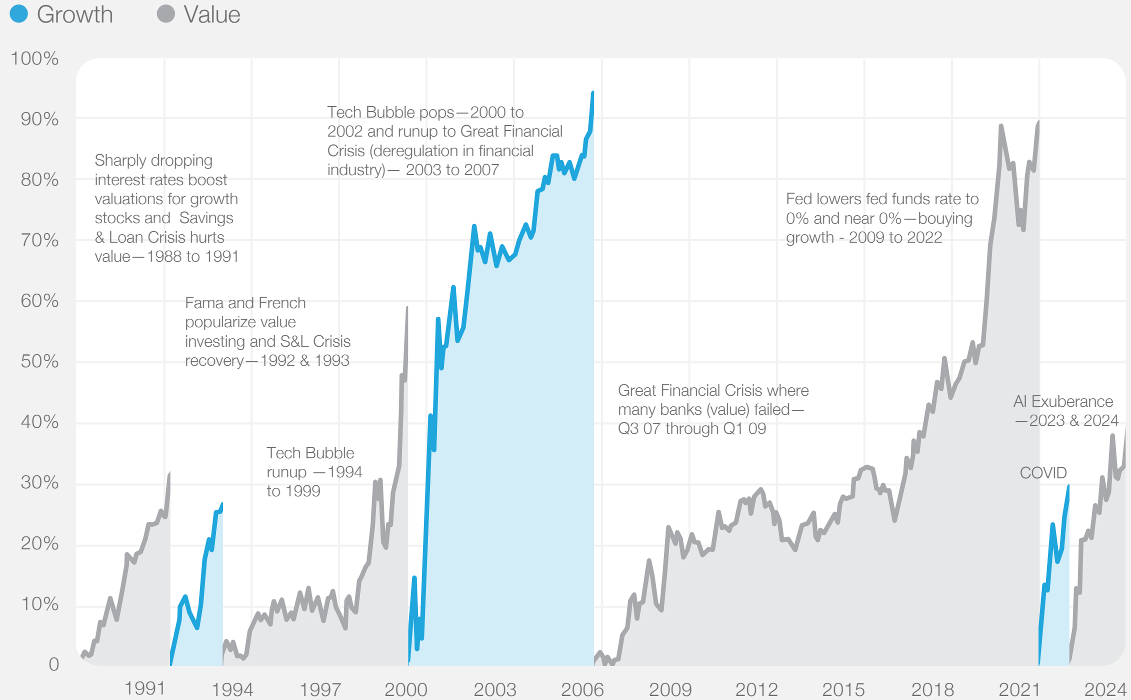
Source: Morningstar

Equities

Despite much uncertainty going into 2024 (election year, generative AI excitement, timing of Fed's actions, etc.), ongoing earnings growth and economic strength buoyed equities throughout the year. The S&P 500 closed at new all-time highs 59 times in 2024 and ended with the 5th best year since 1929. Mid cap and small cap securities also produced returns in 2024 that were above 10%. International equity returns were also positive, although not as much, with International Developed Markets returning 3.8% and Emerging Markets up 7.5%.

Growth continued to dominate over Value in 2024, outperforming by 19%, as AI momentum continued from 2023. Momentum is a market factor that has been shown to occur across growth and value, equity sectors, countries, and individual stocks. The chart below shows how enduring growth's recent outperformance run has been.

Growth vs Value Streaks 9/1/1988 to 12/31/2024*



Asset Class**	Equity Indexes	2024 Returns
Large US Equities	S&P 500	25.0
Large US Growth Equities	Russell 1000 Growth	33.4
Large US Value Equities	Russell 1000 Value	14.4
Mid Cap US Equities	Russell Mid Cap	15.3
Small Cap US Equities	Russell 2000	11.5
International Developed Equities	MSCI EAFE	3.8
Emerging Markets Equities	MSCI Emerging Markets	7.5

* Source: Morningstar
Note: This chart assumes the alpha for growth or value if an investor had rebalanced each month to a neutral allocation. Each of these runs for growth and value would be much larger if we assumed compounding and no rebalancing.

** Source: Morningstar

Overvalued US Equity Market Continues

Among sectors and stocks, 2024 resembled 2023 with growth dominating in large part to the “Magnificent 7” (Apple, Microsoft, Amazon, Alphabet, Tesla, Nvidia and Meta). Collectively, they continue to represent roughly 1/3 of many large cap US equity market-cap weighted indexes. These 7 companies were up 65% in 2024. In 2023, they outperformed the S&P 500 by almost 900bps, returning an average 111% vs. 24% for the index. AI related stocks fall primarily into the Communications and Information Tech sectors.

Financials were close behind AI related stocks with a 30.6% return. Financials benefited from the yield curve’s move from inverted to upward sloping. Traditional banks make money by borrowing on the short end of the yield curve and lending on the long end, so when long term interest rates exceed short term rates, traditional banking tends to do well.

Sectors that are sensitive to higher long-term interest rates underperformed in 2024, as longer term rates climbed, including Real Estate and Energy. The Healthcare sector has been in a funk in 2023 and 2024, after outperforming in 2022, as there has been an increasing backlash against high profits for many drugs and treatments by both Democrats as well as Republicans. Many Materials corporations underperformed because they have operations and sales that are highly international and their profits could be crimped by tariffs.

From a valuation perspective, the S&P 500 continues to be overvalued relative to its history and relative to the 10-year treasury yield, with a P/E ratio of 27.1, up from 24.6 a year ago. Energy is the only sector with a current P/E ratio below its 10-year average. From a profitability perspective, the S&P 500 has grown earnings per share (EPS) by 8.3%, with margin expansion accounting for the majority of the increase. The percentage rise in the S&P 500 this year is greater than earnings percentage growth, resulting in higher valuations.

S&P 500 Sector Index	2024 Returns
Communication Services	40.2
Information Technology	36.6
Financials	30.6
Consumer Discretionary	30.1
Utilities	23.4
Industrials	17.5
Consumer Staples	14.9
Energy	5.7
Real Estate	5.2
Health Care	2.6
Materials	0.0

Source: Morningstar

Although the Energy sector has a lower P/E than other sectors, we are concerned about Energy related stock profits for the next few years, as Trump has promised to change regulations to make it easier to produce oil in the US. As supply increases, oil prices typically decrease and Energy producer profits should drop.

Strength of the US Dollar

The US Dollar has been widely used as the world's reserve currency since the end of World War II. It is still the majority of global reserves held in central banks, but a 2024 Brookings Institution report showed that the Dollar's share of global reserves had declined to 59% from 70% in 2000.

Since 2011, the Dollar has strengthened and is now at a more appreciated level than at any time since the Plaza Accord in 1985, when a joint agreement was signed by the world's leading trading countries to devalue the US Dollar. It has only been higher in four previous months. Today, the US Dollar is currently up 5% versus developed and 4% versus emerging trading partners since early October. Despite Trump's preference to support domestic manufacturers and impose tariffs on countries that seek to replace the dollar in trade, his policies may have the opposite effect, strengthening the already overvalued US Dollar.

Looking Ahead at Small Caps

Unlike Large Cap companies that often are multinational with exposure outside the US, Small Cap companies tend to be more domestically focused. Therefore, they are less affected by international trade or currency fluctuations. Historically, Small Caps tend to outperform following a presidential election and this year is no exception. Small Caps were up 11% in November, outpacing Large Caps and Mid Caps by over 200bps and 500bps respectively. Small Caps are also more sensitive to interest rates than Large Cap companies, and increasing interest rates in December erased a large part of Small Caps' gain.

Looking ahead, potential higher tariffs on imports may bode well for smaller companies if imports are more expensive, renewing an interest for domestically produced goods. In addition, smaller companies may have increased pricing power from reduced competition from imports. This may lead to smaller companies improving profit margins with better overall financial performance, in addition to capturing a greater share of the market. By many metrics, Small Cap Value is currently trading at significantly more attractive valuations than larger cap companies and Advyzon Investment Management has an overweight to Small Cap US Value stocks.

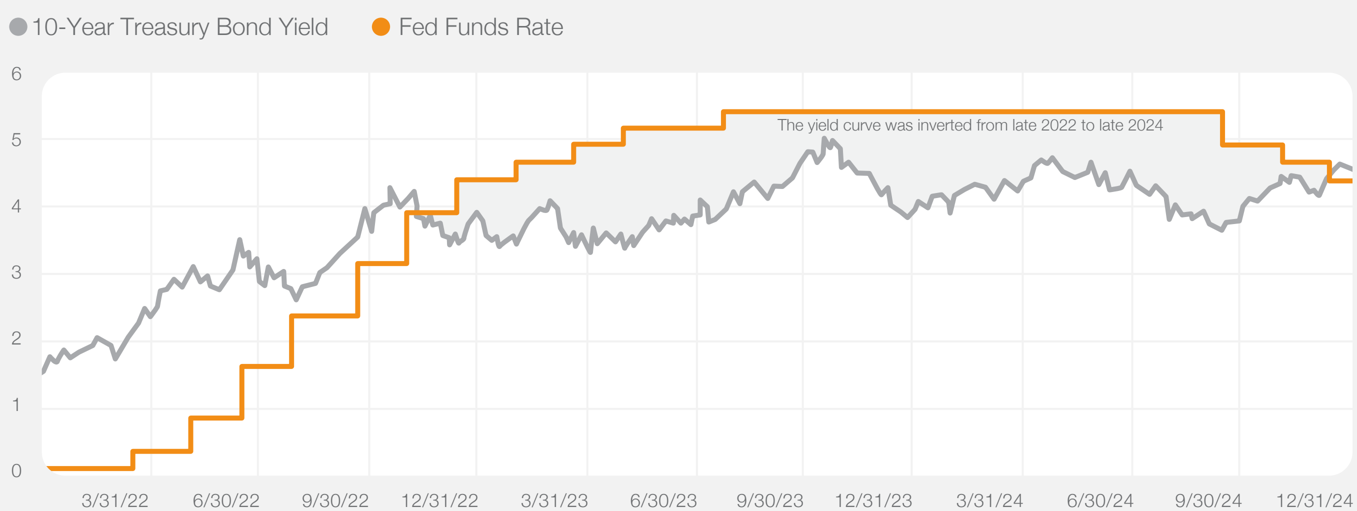
"By many metrics, Small Cap Value is currently trading at significantly more attractive valuations than larger cap companies…

Fixed Income

The popular Bloomberg Barclays US Aggregate Bond Index generated a total return of 1.3% in 2024, comprised of a coupon yield of +3.7% and a price change of -2.4%. That total return was below its long run average total return of 6.8% (between 1976 and 2023), the fourth consecutive year of below average returns for intermediate bonds. Longer term bonds fared worse, as both long term treasuries and long term corporate bonds had negative total returns.

2024 started with a deeply inverted yield curve, with 10-year bonds yielding 1.5% less than the mid-point of the Federal Reserve's overnight lending rate. The Fed lowered their overnight rate by 1.0% in the last few months of 2024 from a mid-point of 5.375% to 4.375%, while the yield on a 10-year treasury bond increased by 0.70% from 3.87% to 4.57%. That left the curve spread at 12/31/24 between a 10-year treasury and the Fed Funds rate at +0.20%, a much more typical spread we see with an upwardly sloping yield curve. The three-year chart below helps put this regime shift and duration of the inverted yield curve into perspective. The yield curve reverted back to a positive slope on 12/17/2024, the day of the Fed's most recent meeting and overnight lending rate reduction.

10-Year Treasury Yield and Fed Funds Rate—1/1/22 to 12/31/2024 (Since "Liftoff")



Source: Federal Reserve Bank of St. Louis—https://fred.stlouisfed.org

Fixed Income

An inverted yield curve often portends a recession, because the longer end of the yield curve drops on 1) investor expectations that the Fed may eventually lower short term rates to spur a flagging economy and 2) buying of treasury bonds as investors shift allocations out of equities and into bonds in a defensive repositioning. During the inversion of Q4 2022 to Q4 2024, this was not the case. The yield curve inverted during this recent period because the Fed moved short term rates to a relatively high level to fight inflation caused primarily by energy prices that had climbed as a result of Russia's invasion of Ukraine. Many forecasters called for a recession in 2023 and 2024 when they saw the inverted yield curve at 12/31/22, but they were not considering the context of the inversion and the recession did not materialize.

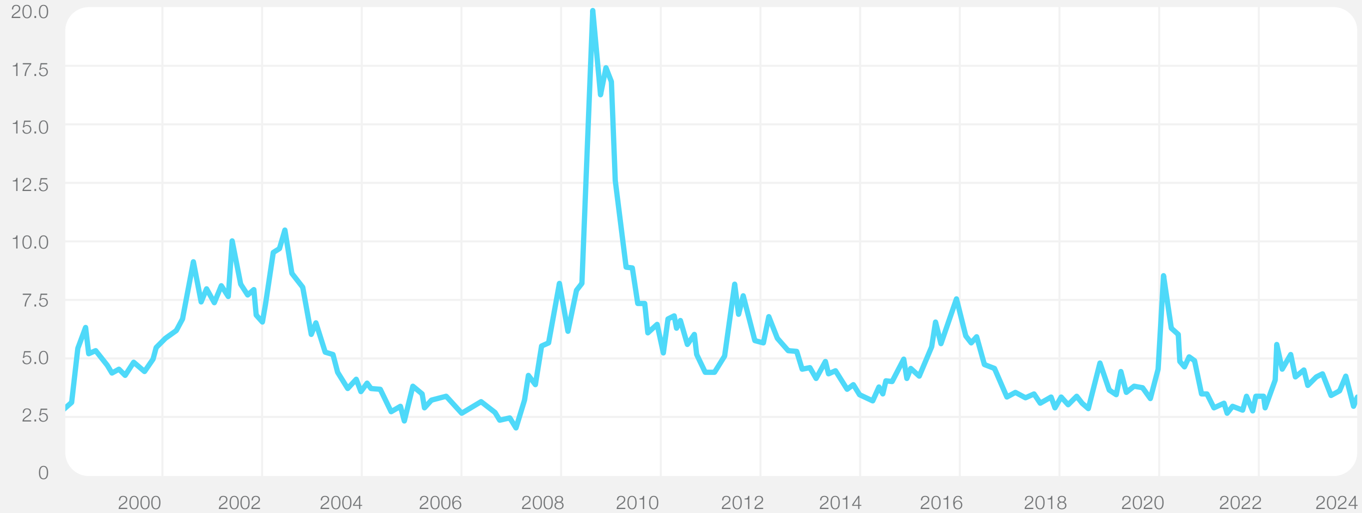
Investors who overweighted shorter term bonds and underweighted longer term bonds were rewarded with higher total returns during the last three years. Now that the yield curve has returned to a more normal, upward slope, we are comfortable buying back into the riskier, long term end of the curve—in October 2024 we added long term bond exposure in our Advyzon Asset Allocation portfolios.

Asset Class	Index Name	2022 Total Return	2023 Total Return	2024 Total Return	3-Year Ann. Total Return at 12/31/24
Long Term Bonds	Bloomberg US Govt/Credit Long	-27.1	7.1	-4.2	-9.2
Intermediate Term Bonds	Bloomberg US Agg Bond	-13.0	5.5	1.3	-2.4
Short Term Bonds	Bloomberg US Govt/Credit 1-3 Yr	-3.7	4.6	4.4	1.7
Cash	ICE BofA US 3M Trsy Bill	1.5	5.0	5.3	3.9

Source: Morningstar

> "Now that the yield curve has returned to a more normal, upward slope, we are comfortable buying back into the riskier, long term end of the curve…

ICE BofA US High Yield Index Option-Adjusted Spread



Source: Ice Data Indices, LLC

Now that the yield curve is upward sloping again and yields on intermediate bonds are much closer to their long run average (which was 4.81% for the 40 years between 1985 and 2024), we expect intermediate bonds to generate a return in the 4% to 5% range in 2025. We expect long term bonds to have returns slightly higher than intermediate bonds.

High yield credit spreads have been dropping since July 2022 and ended 2024 at levels that are well below long run average levels. Historically, starting a period with low credit spreads (below 4%) has augured below average returns during the next couple years and may suggest reducing high yield bond allocations. At 12/31/24, the high yield credit spread was 2.9%.

Fixed Income

Among bond sectors, credit related bonds have outperformed in recent years producing slightly positive performance over the last three years. Government and mortgage backed bonds have had negative performance, as their coupons do not include as much of a premium for the risk of default.

We expect credit bonds to continue to have the best performance among bond sectors, but we expect mortgage backed bonds to outperform treasuries for the next few years. Mortgage rates are more likely to decrease than they are to increase, which should provide a tailwind to MBS bonds. At the same time, because the US federal deficit has reached astronomical levels and Trump showed no interest in decreasing the debt during his first term, we may see heavy issuance for treasuries and commensurate price pressure, leading to lackluster returns for treasuries.

During our annual review of holdings across all accounts in our Advyzon database, we noted during the last couple years that Certificates of Deposit saw significantly increased allocations, as many shorter term CDs sported yields above 5%. Banks and Credit Unions are no longer offering rates this high, as their CD rates are highly correlated with the Fed's overnight lending rate, which has dropped 1%. We expect to see CD allocations drop, in favor of higher yielding intermediate and long term bonds.

> "We expect credit bonds to continue to have the best performance among bond sectors…

Bond Sector	Index Name	2022 Return	2023 Return	2024 Return	3-Year Ann. Return at 12/31/24
Credit	Bloomberg US Intermediate Credit	-9.1	6.9	4.0	0.4
Government	Bloomberg US Govt Intermediate	-7.7	4.3	2.4	-0.5
Mortgage Backed	Bloomberg US MBS	-11.8	5.0	1.2	-2.1

Source: Morningstar

Asset Allocation

Asset Allocation typically refers to the percentages that an investor assigns to a set of asset classes. The Advyzon Investment Management team manages multiple sets of asset allocation portfolios that span a broad spectrum of risk and return target levels, with nine portfolios that span 20% equity up to 98% equity at 10% intervals. The primary reason an investor uses asset allocation portfolios is to benefit from the diversification and the risk reduction these portfolios offer when the asset allocation is done skillfully. A diversified portfolio with 60% total equity and 40% bond exposure is often used as a benchmark for asset allocation portfolios, as it offers an attractive risk and return tradeoff for a broad set of investors.

The “quilt chart” to the right shows the last twelve calendar year results for eight asset classes and one diversified portfolio that combines the eight asset classes into a portfolio with an overall 60/40 stock and bond mix (see the disclosures at the end of this writeup to see the exact allocations and indexes we used to build the diversified portfolio). Each investment option holds its color from left to right and each column/year is sorted from highest return to lowest. The chart also includes a period return (not annualized) for all twelve years in the right column.

Annual Return Quilt Chart For Asset Classes and a Diversified Portfolio

	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024	2013–2024
Higher Return	Small US stocks 38.8	LT Treas bonds 25.1	Large US stocks 1.4	Small US stocks 21.3	Emerging Mkt stocks 37.3	3 Month T-bills 1.9	Large US stocks 31.5	Small US stocks 20.0	Large US stocks 28.7	3 Month T-bills 1.5	Large US stocks 26.3	Large US stocks 25.0	Large US stocks 415.6
	Large US stocks 32.4	Large US stocks 13.7	Interm bonds 0.5	High Yld bonds 17.1	Int'l stocks 25.0	Interm bonds 0.0	Small US stocks 25.5	Large US stocks 18.4	Small US stocks 14.8	High Yld bonds -11.2	Int'l stocks 18.2	Small US stocks 11.5	Small US stocks 200.9
	Int'l stocks 22.8	Diversifed portfolio 7.2	3 Month T-bills 0.1	Large US stocks 12.0	Large US stocks 21.8	LT Treas bonds -1.8	Int'l stocks 22.0	Emerging Mkt stocks 18.3	Diversifed portfolio 11.7	Interm bonds -13.0	Small US stocks 16.9	Diversifed portfolio 10.7	Diversifed portfolio 138.1
	Diversifed portfolio 15.8	Interm bonds 6.0	Int'l stocks -0.8	Emerging Mkt stocks 11.2	Diversifed portfolio 16.0	High Yld bonds -2.1	Diversifed portfolio 20.6	LT Treas bonds 17.7	Int'l stocks 11.3	Int'l stocks -14.5	Diversifed portfolio 15.7	High Yld bonds 8.2	Int'l stocks 93.8
	High Yld bonds 7.4	Small US stocks 4.9	Diversifed portfolio -1.2	Diversifed portfolio 8.4	Small US stocks 14.6	Large US stocks -4.4	Emerging Mkt stocks 18.4	Diversifed portfolio 13.2	High Yld bonds 5.3	Diversifed portfolio -16.5	High Yld bonds 13.4	Emerging Mkt stocks 7.5	High Yld bonds 82.2
	3 Month T-bills 0.1	High Yld bonds 2.5	LT Treas bonds -1.2	Interm bonds 2.6	LT Treas bonds 8.5	Diversifed portfolio -5.3	LT Treas bonds 14.8	Int'l stocks 7.8	3 Month T-bills 0.1	Large US stocks -18.1	Emerging Mkt stocks 9.8	3 Month T-bills 5.3	Emerging Mkt stocks 36.2
	Interm bonds -2.0	3 Month T-bills 0.0	Small US stocks -4.4	LT Treas bonds 1.3	High Yld bonds 7.5	Small US stocks -11.0	High Yld bonds 14.3	Interm bonds 7.5	Interm bonds -1.5	Emerging Mkt stocks -20.1	Interm bonds 5.5	Int'l stocks 3.8	3 Month T-bills 19.3
	Emerging Mkt stocks -2.6	Emerging Mkt stocks -2.2	High Yld bonds -4.5	Int'l stocks 1.0	Interm bonds 3.5	Int'l stocks -13.8	Interm bonds 8.7	High Yld bonds 7.1	Emerging Mkt stocks -2.5	Small US stocks -20.4	3 Month T-bills 5.0	Interm bonds 1.3	Interm bonds 18.7
Lower Return	LT Treas bonds -12.7	Int'l stocks -4.8	Emerging Mkt stocks -14.9	3 Month T-bills 0.3	3 Month T-bills 0.9	Emerging Mkt stocks -14.6	3 Month T-bills 2.3	3 Month T-bills 0.7	LT Treas bonds -4.7	LT Treas bonds -29.7	LT Treas bonds 3.1	LT Treas bonds -6.4	LT Treas bonds 2.4

Source of returns: Morningstar

While each of the individual asset classes bounce up and down significantly from year to year, the diversified portfolio gives a smoother result, staying between the 3rd and 6th rows, and ending up on the 3rd row for the combined 12-year period on the right.

The 60/40 portfolio is occasionally maligned in the press as "out of date" or simply "dead." Usually, authors of these articles have an ulterior sales motive—often pushing a complex "low volatility" strategy or maybe a more exotic derivative-based hedge fund like "risk parity" or "VIX-hedged" strategies. Since the tech bubble of the late 1990s, we have seen hundreds of these exotic strategies gain popularity temporarily after a market pullback, only to hit an "unexpected" combination of market events that blows up their strategy (creating unacceptably large losses) that was "thoroughly backtested with a quantum computer and 100 million market simulations." Adding additional headwinds to the efforts of these strategies is a typically high expense ratio. Over the long run, we have not found a derivative based strategy that outperforms straightforward, inexpensive market beta and good diversification with some thoughtful portfolio tilting (whether it is quantitative based or fundamental sourced at the security level or asset class level).

The table below has return and risk metrics in rows by decade for the same diversified 60/40 portfolio we used in the quilt chart above. We include returns for US inflation and risk metrics for the S&P 500 stock index for comparison. The non-US equity index that is part of our diversified 60/40 asset allocation portfolio has the shortest history and constrains us to reviewing hypothetical return information back to January 1, 1988. The first and last rows of data are for partial decades.

		Metrics for 60/40 Diversified Portfolio				Metrics for Comparison		
Decade	**Months in Period**	**Period Return**	**Annualized Geometric Return**	**Annualized Monthly Std. Deviation**	**Maximum Drawdown in Period**	**Ann. Inflation in Period**	**S&P 500 Ann. Monthly Std. Deviation**	**S&P 500 Max. Drawdown in Period**
Jan 1988 to Dec 1989	24	42.8%	19.5%	6.9%	-2.4%	4.5%	11.2%	-3.8%
Jan 1990 to Dec 1999	120	221.7%	12.4%	8.9%	-11.9%	2.9%	13.4%	-15.4%
Jan 2000 to Dec 2009	120	45.8%	3.8%	10.9%	-35.9%	2.5%	16.1%	-50.9%
Jan 2010 to Dec 2019	120	129.2%	8.6%	7.9%	-10.2%	1.8%	12.5%	-16.3%
Jan 2020 to Dec 2024	60	36.3%	6.4%	12.8%	-21.5%	4.2%	18.2%	-23.9%

Source of returns: Morningstar

One goal of the 60/40 portfolio is to produce a total return that beats inflation. Our sample 60/40 portfolio does that over all 5 time periods. The 60/40 portfolio beats inflation over most rolling periods of at least one year. The longer the rolling period you use, the more likely the diversified portfolio's return is to beat inflation. Another goal for our 60/40 portfolio is to tamp risk down meaningfully versus the S&P 500 index. The 60/40 portfolio achieves this with a much lower standard deviation and drawdown than the S&P 500 index in each row.

Alternative investments can help increase return or reduce risk for asset allocation portfolios but it takes skill and sometimes luck to be able to add alternatives at the right time, in the right amount, and sourced from the right asset classes. Many alternative asset classes can exhibit extreme drawdowns and can be expensive. Sometimes investors use publicly traded, liquid alternatives and some use private, illiquid investments that require the investor to be accredited. It is important to source the allocations properly—if you are adding a higher risk, higher return diversifier, it makes sense to source the allocation from equities. If you are adding a lower risk, lower returning diversifier, source it from bonds.

Many investors make the mistake of sourcing all alternative allocations from equities, and then ending up with a much lower return than an investment policy statement calls for.

When using alternatives in a portfolio, we recommend being active and thoughtful with your allocations. At the end of 2024, we are facing relatively high valuations for US stocks, making

> “…we would be more likely to use higher risk, higher return alternatives in place of some traditional stock exposure today…

them relatively less attractive than they would be otherwise and lowering our short term return expectations. At the same time, we are facing attractive intermediate and longer term bond yields. For that reason, we would be more likely to use higher risk, higher return alternatives in place of some traditional stock exposure today, and we would be less likely to allocate to safer alternative options with bond-like returns.

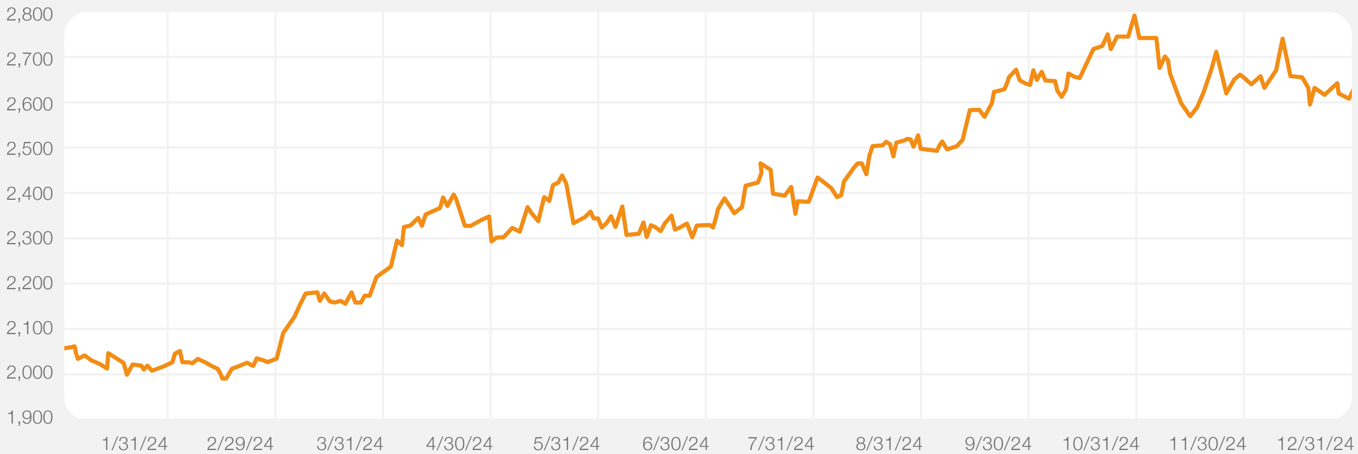
Alternatives

Gold and Silver

Precious metals are the defining real asset from the very beginnings of human civilization. Gold and silver have been recognized for their intrinsic value and utility as a store of value for over 5,000 years. Gold, in particular, has endured as a safe haven and store of value. In recent years interest in the yellow metal has increased as the worldwide embrace of fiat currency, where all major sovereign currencies have no connection whatsoever to gold, has become increasingly entrenched. The US Dollar's last connection to gold ended in 1971 with President Nixon's full closing of the gold window. Switzerland followed suit in 1999 severing its Swiss francs last connection to gold.

Gold rose sharply in 2024 with gold spot price rising from $2,062/troy oz to more than $2,780 in late October, and ultimately pulling back to $2,629/troy oz at the end of December. That was a 27.5% return and the 5th highest return in the last 50 years. Economic uncertainty and global conflict came together to drive gold prices upward. A perception of the eventual weakening of the US Dollar due to a potential return to monetary easing and the ongoing ballooning of US deficit and debt metrics also contributed. Both individual investor and central bank buying (particularly in Turkey, India, and other emerging countries) bid gold prices upward.

Prices for Gold During 2024



Source: Yahoo Finance

Prices for Silver During 2024

Source: Yahoo Finance

Silver also rose sharply in 2024, opening the year with spot price of $23.85/troy oz to more than $34.80 in late October, and ultimately pulling back to $28.94 at the end of December. That was a 21.3% return and the 13th highest return in the last 50 years. The white metal's near $35/oz pricing in October was its highest price since its mercurial spike upward in 2010–2011. The big spike in silver prices was driven by similar factors to gold, plus an increase in industrial demand which often plays a more important role in the price of silver than gold.

Gold and silver remain attractive diversification options for modest allocations in an investment portfolio and a viable check on inflation and the potential decreasing purchasing powers of the various sovereign fiat currencies. Additionally, many of the factors driving the upward trend in precious metal prices may persist. That said, unlike stocks, bonds, and other investments, precious metals create no cash flow. The metals also experience periods of high volatility.

Global Infrastructure

Global infrastructure is a grouping of companies domiciled across the globe that own and operate physical infrastructure in energy, transportation, and utilities like power plants, roads, bridges, water treatment facilities, etc. Investors in global infrastructure gain access to essential infrastructure across the world. The asset class is sought for its potential to generate stable cash flows and its inflation-hedging characteristics.

In 2024, global infrastructure represented by the S&P Global Infrastructure Index rose by almost 20% through November but pulled back 4.5% in December.

1 Year Total Return (12/31/24)

S&P Global Infrastructure Index	15.1

Source: Morningstar

Despite an uncertain interest rate environment, several tailwinds helped drive global infrastructure returns upward. A robust North American energy supply with a growing potential for export capacity helped on the midstream energy front. Additionally, utilities continue to benefit from continued increases in electrification and digital computing demand.

The need for continued infrastructure improvement and the ability to pass through potential higher inflation to increase revenues make global infrastructure a potentially attractive investment and inflation hedge going forward.

Commodities

Commodities are basic goods like oil, grains, livestock, etc. that are essential to worldwide commerce and trade. Modestly falling oil prices drove softer gains for commodities than other real assets in 2024 through the end of the year.

1 Year Total Return (12/31/24)

Bloomberg Commodity Index	5.4

Source: Morningstar

A glut of oil supply could be a headwind for commodities prices in 2025. Trump's "Drill, baby, drill" mandate has the potential to flood the market with oil, pushing prices down to the $20 to $40 range like we saw during much of 2020 during Trump's first presidency. This would be disastrous for profits of oil producing companies, but good for US citizens and companies that purchase oil for personal use or as an input for production of other finished goods or utilities. Some analysts are concerned that some of Trump's mandates could drive higher inflation for many products and commodities can make an attractive hedge against inflation.

"A glut of oil supply could be a headwind for commodities prices in 2025.

Other Alternatives

The seven additional alternative investments listed below are other alternative investments that are relatively popular with investors and are available in easy to trade liquid fund formats. They can be attractive, diversifying additions to portfolios in small amounts, but are usually not worth adding to portfolios under $200k because the typical allocation level would be de minimis. Each of these investment types can lower risk through a correlation of less than 1 with stocks and bonds, but they can have extreme results on an annual basis and should typically be used in very limited amounts. We show the last three annual returns next to results for the S&P 500 index to demonstrate how the returns can add significant tracking error versus a portfolio's benchmark.

Among these seven investment types, the most attractive to us right now is Bitcoin for multiple reasons. Although it has gone up significantly during the last two years, it has such a high upside, it may be worth the risk of a drawdown for a small allocation. A looser regulatory environment (not just in the US, but abroad as well) would be a tailwind for all cryptocurrency securities. If the US Dollar has a reversion to the mean after its recent runup, Bitcoin might be an attractive store of wealth for some investors. Finally, momentum is a strong market factor when looking back twelve months, and Bitcoin has had very high returns over this lookback window.

Indexes	2022 Return	2023 Return	2024 Return
S&P 500	-18.1	26.3	25.0
Red Rocks Gbl Listed Private Eqty	-36.4	38.5	17.9
ICE BofA All US Convertible	-18.7	12.9	11.1
S&P Preferred Stock	-18.9	12.0	9.2
Alerian MLP	30.9	26.6	24.4
FTSE NAREIT All Mortgage Capped	-27.0	15.1	-0.2
Credit Suisse Managed Futures	18.6	-2.8	1.0
CMBI Bitcoin	-64.0	57.0	120.0

Source: Morningstar

The second most attractive investment today among this group is mortgage REITs (represented by the FTSE NAREIT All Mortgage Capped TR index). These securities have experienced weakness over the last few years as mortgage rates rose. We expect the worst is over for mortgage rates, which clears the way for this asset class to potentially produce high single digit or low double digit returns until we encounter a new market regime.

Disclosures

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Cryptocurrencies, including Bitcoin, are currently unregulated, illiquid, uninsured, carry technological risks, require unique tax treatment, and are volatile.

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Disclosures

The Diversified portfolio in the quilt chart on page 15 is comprised of a weighted average of: 33% Large US stocks represented by the S&P 500 index, 7% Small US stocks represented by the Russell 2000 index, 14% International stocks represented by the MSCI EAFE index, 6% Emerging Market stocks represented by the MSCI EM index, 8% High Yield bonds represented by the Bloomberg US Corporate High Yield index, 6% Long Term Treasury bonds represented by the Bloomberg Long Term US Treasury index, 25% Intermediate bonds represented by the Bloomberg US Agg Bond index, 1% 3 Month T-bills are represented by the ICE BofA US 3M Trsy Bill index.

Definitions of Indexes Used:

S&P 500 Index: A market capitalization-weighted index that tracks the performance of 500 of the largest publicly traded companies in the United States. It is widely regarded as one of the best benchmarks of the overall U.S. stock market and economy, as it encompasses companies across 11 sectors, including technology, healthcare, financials, and consumer goods.

Russell 2000 Index: A stock market index that measures the performance of approximately 2,000 small-cap publicly traded companies in the United States. It is a subset of the larger Russell 3000 Index, which includes the 3,000 largest U.S. stocks, making the Russell 2000 a widely recognized benchmark for small-cap stocks.

MSCI EAFE Index (Morgan Stanley Capital International Europe, Australasia, and Far East Index): A widely recognized benchmark that tracks the equity market performance of developed markets outside of the United States and Canada. It includes companies from 21 countries across Europe, Asia, and the Pacific regions.

MSCI EM Index (Morgan Stanley Capital International Emerging Markets Index): A widely used benchmark that tracks the equity market performance of emerging market (EM) economies. It provides a comprehensive representation of stock market performance across 24 emerging countries, focusing on large- and mid-cap companies.

Bloomberg US Corporate High Yield Index: A market-value-weighted benchmark that measures the performance of U.S. dollar-denominated, non-investment-grade corporate bonds. These bonds, commonly referred to as "junk bonds," offer higher yields due to their higher credit risk compared to investment-grade bonds.

Bloomberg US Agg Bond Index: A comprehensive, market-value-weighted index that measures the performance of the U.S. investment-grade bond market. It is one of the most widely used benchmarks for fixed-income investors.

ICE BofA US 3M Treasury Bill Index: A benchmark that tracks the performance of U.S. Treasury bills with a remaining maturity of three months. It is widely used as a proxy for short-term, risk-free interest rates and serves as a key benchmark for cash and cash-equivalent investments.

Advyzon
INVESTMENT MANAGEMENT

For additional information, please call or email:
(844) 829-0039 | Sales@AdvyzonIM.com | AdvyzonIM.com

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