MONONGAHELA CAPITAL MANAGEMENT

PERCEPTIONS

2nd Quarter, June 30, 2024	06/30/2024	% Change 2nd Quarter	% Change Year to Date
Dow Jones Industrial Average	39,118.86	-1.27 %*	4.79 %*
S&P 500	5,460.48	4.28 %*	15.29 %*
Russell 2000	2,047.69	-3.28 %*	1.73 %*
Bloomberg Aggregate Bond Index		0.07 %	-0.71 %
10 Year Treasury Yield	4.40 %		
30 Year Treasury Yield	4.56 %		

** Includes reinvested dividend*

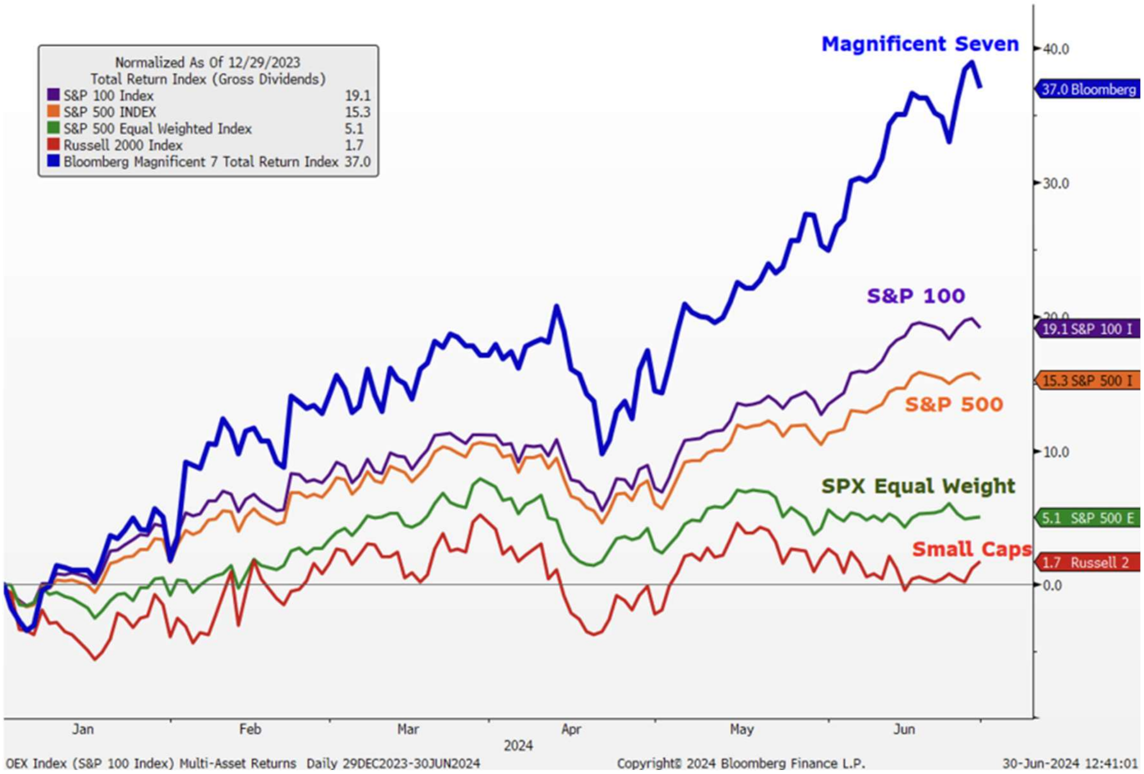
Crowded Trades and Bifurcated Markets

While the headline reports for the 2nd quarter market returns were portrayed as very positive, we found it interesting to note the market dispersion in total returns across various major indices. In the 2nd quarter, the S&P 500 gained 4.3% whereas the Dow Jones Industrial Average lost 1.3% and the Russell 2000 fell 3.3%. The absolute spread between the indices' performances is even greater in the first half of the year. The S&P 500 rose 15.3% while the Dow Jones Industrial Average and Russell 2000 grew 4.8% and 1.7% respectively.

Although these figures may at first glance suggest a broad outperformance by the constituents of the S&P 500, a more granular examination reveals the S&P 500's return was significantly influenced by its outsized weighting in the Magnificent Seven (or the Mag 7 for short). The Seven include Apple, Microsoft, Google, Amazon, Nvidia, Meta Platforms, and Tesla. Their performance in the first half of 2024 represents approximately $4.2 trillion or approximately 67% of the $6.2 trillion increase in the S&P 500 market value. This massive appreciation of capital is highlighted by the chart on the following page. The surge in the first six-months of this year is on top of a Mag 7 outperformance in 2023. The S&P 500 was up 26.2% in 2023 while the S&P Equal Weight Index was up 13.8% (the difference reflecting the outsized weighting of the Mag 7).

When reviewing historical performances, there are certain patterns of trading on Wall Street that are immutable. Bob Farrell, a respected analyst for Merrill Lynch and one of the first technicians to incorporate behavioral science into his analytical work, published "Market Rules to Remember" (Ten Rules) towards the end of his career in 1998. Considering the bifurcation in today's equity markets, we found it appropriate to review his third rule:

Rule # 3. There are no new eras — excesses are never permanent.



While the Seven represent outstanding companies, their outsized returns have consequently created benchmark performance pressures. The mass movement of funds into the Mag 7 is a perfect example of a crowded trade. These flows occur when multiple participants chase a similar strategy, and this method works well amid a bull market with ample liquidity. However, when the equity position or positions moves out of favor, and at some point, they do, the mass rush to the exit can result in liquidity shortages and sharp selloffs.

We would posit that at some point, the allocation of funds into the Mag 7 may slow or reverse, and the risk to the downside is significant. Historically speaking, market trends tend to revert to the mean over time, and we are currently in a particular period of extreme concentration in a select few equities. A reversion would result in a flattening or declining return by the Mag 7 and an opportunity for a relative outperformance by broader markets, like the Russell 2000 and the S&P 500 EWI, which have largely been left behind.

We continue to rebalance your portfolio, adjusting positions that have done very well but may now be overweighted or significantly above our intrinsic value price. The extreme concentration in so few stocks (excesses) is not permanent. Identifying and understanding the risk associated with crowded trades and reducing exposure will increase your liquidity, allowing for allocation to lower risk opportunities in the underperforming components of the Russell 2000, S&P 500, and Treasuries.

Definitions

Russell 2000 Index is a market-capitalization-weighted index and represents the common benchmark for small capitalization stocks. It represents 2,000 of the smaller companies in the broad Russell 3000 Index.

The S&P 500 Index represents the leading 500 companies in the U.S. and emphasizes market capitalization. The return is based on the total market capitalization of its components, with larger companies garnering more weighting.

The S&P 500 Equal Weighted Index (EWI) includes the same stocks as the S&P 500, but each company in the EWI has an equal weight, 0.2%.