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RIVERBRIDGE QUARTERLY

1ST QUARTER 2024

MARKET COMMENTARY

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The first quarter of 2024 built on the strength of last year by posting a gain of more than 10 percent for the S&P 500 index, the best opening quarter for the equity market since 2019. Stronger-than-expected corporate earnings drove stocks higher, with assistance from continued artificial intelligence momentum and economic data that generally suggested inflation should continue to cool. Whether the markets will continue ascending for the remainder of the year will likely be predicated on corporate earnings. Additionally, investors will need to navigate potential volatility caused by the timing of rate cuts by the Federal Reserve, a presidential election, and the overall health of the consumer.

Several of the factors that propelled the stock market to outsized returns in 2023 persisted into the new year, including continued excitement surrounding artificial intelligence, anticipation of interest rate cuts, inflation trending lower, and few signs of an imminent economic downturn. Unquestionably, however, corporate earnings provided the biggest boost to first quarter returns. Fourth quarter 2023 earnings, reported in the first quarter of 2024, grew more than 10 percent, according to FactSet. Investors had expected 4.7 percent growth entering earnings season. This double-digit earnings growth not only generated optimism but also helped to justify the valuation of many stocks reaching new highs.

Paradoxically, this market advance did not receive much help from the Fed. As the year began, investors expected six interest rate cuts in 2024, with the first in March. Due to better-than-expected reported economic data, the Fed has lowered these expectations and delayed the timing of potential cuts. Currently, the markets are pricing in three rate cuts, with the first in June or possibly July. This shift in expectations caused the yield on the 10-year U.S. Treasury to rise to 4.192 percent from 3.860 percent at the beginning of the year. Over the past five years, it has been somewhat unusual for the equity markets to post gains during periods of rising interest rates.

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As Riverbridge looks ahead, we are optimistic about the prospects of our portfolio companies. We believe they are positioned well for growth, regardless of the economic backdrop. Recently, there has been a sharp increase market-wide in the number of companies defaulting on their debt. Our insistence that our portfolio companies be capable of internally financing their growth should shield our portfolios from this concerning phenomenon and provide greater earnings power durability.

Over the last five years, the equity markets have experienced numerous market-shaping events that defy anyone's predictive abilities. However, what remains true is that earnings power determines the value of companies. Management teams that focused on building their strategic market positions throughout this highly disrupted period have benefited most. Those management teams more focused on maximizing performance by capitalizing on a small moment in time have generally underperformed. The Riverbridge investment team will continue to eschew the short-lived emotions of the market and focus on companies that are positioning themselves to thrive over the next decade.