WELLS FARGO
Investment Institute

Investment Strategy

Weekly guidance from our Investment Strategy Committee **April 15, 2024**

Alternatives Spotlight: The value of alternative investments 2

- Alternative investments continued to gain traction by offering greater diversification benefits and differentiated strategies.
- New strategies and semi-liquid products have also been developed in recent years to satisfy the needs of high-net-worth investors.

Equities: Target change recap 4

- A boost to the U.S. economic outlook and continued easy financial market conditions have led us to re-rate our 2024 U.S. equity market earnings and price targets.
- For 2025, we look for stronger earnings growth with correspondingly higher price targets, for all global equity asset classes.

Fixed Income: 10-year yields – A look back 5

- We are most favorable short-term fixed income as the Federal Reserve (Fed) remains on pause, for now; should long-term interest rates test the upper end of our 2024 year-end target range of 4.25%-4.75% we would encourage income-oriented investors to consider locking in rates in longer maturities.
- We recently changed our 2024 year-end federal funds rate expectations from three 0.25% rate cuts to two, and initiated our 2025 year-end expectations, which anticipate one additional rate cut.

Real Assets: Gold hitting new all-time highs – Raising targets 6

- The price of gold hit an all-time high of $2,353 per troy ounce last week — up now 14% on the year.
- We are raising our 2024 forecast to $2,300 – $2,400 per troy ounce, and initiating our 2025 target range at $2,400 – $2,500 per troy ounce.

Current tactical guidance 7

Investment and Insurance Products: ➤ NOT FDIC Insured ➤ NO Bank Guarantee ➤ MAY Lose Value

© 2024 Wells Fargo Investment Institute. All rights reserved.

Alternatives Spotlight

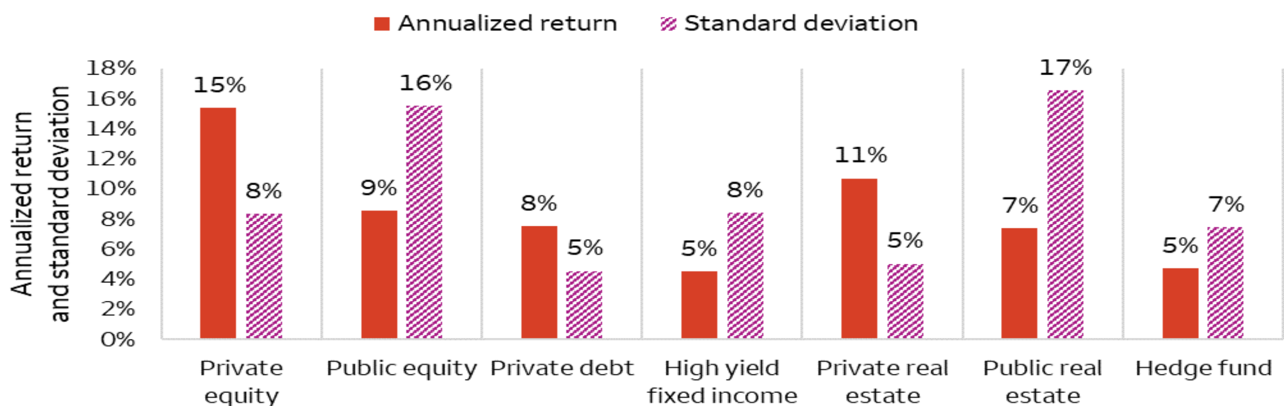
Chao Ma, PhD, CFA, FRM
Global Portfolio and Investment Strategist

The value potential of alternative investments

Alternative investments, including private capital and hedge funds, continued to gain traction among high-net-worth investors. According to Preqin, private capital asset under management has soared from under $1 trillion in 2003 to over $15 trillion in 2023. Many qualified investors are drawn to alternatives for potential diversification benefits and differentiated strategies available.

- Diversification benefits: Alternative investments often focus on opportunities not available in public markets. For example, private equity and private credit managers own or lend to privately held companies that are not traded on stock exchanges. These companies jointly account for a majority of companies created and represent diverse industries and sectors. This feature contrasts with a shrinking public market universe, the returns of which are increasingly driven by a handful of mega-cap technology companies in recent years. Alternatives' diversification benefit potential are also evidenced by a lower correlation to public assets and a lower return standard deviation (volatility) compared with similar public assets (chart 1). These diversification attributes can help mitigate pullbacks in public markets and thereby smooth an investor's return experience.
- Differentiated value propositions: Venture capital may enjoy favorable return potential, and private debt may offer incomes, as they capitalize on taking ownership of early-stage, high-growth companies or financing mid-sized companies. In contrast, infrastructure strategies provide investors access to public service entities' stable cash flows, characterized by limited competition and relatively inelastic demand. Therefore, infrastructure returns are often defensive to economic downturns and can offer a buffer from elevated inflation. This diverse set of investment opportunities is also reflected in the wide range of historical returns. As shown in chart 1, Private Equity led the group with an impressive 15% average return over the 10-year period ending September 30, 2023, followed by other private capital asset classes' near 10% annual profits, with many of them outperforming similar public assets.

Chart 1. Historical private and public asset class average return and standard deviation



Sources: Wells Fargo Investment Institute, Pitchbook, and Bloomberg. Data as of September 30, 2023. Average annualized returns depicted are calculated over a 10-year period spanning Q4 2013 to Q3 2023. Private equities: Pitchbook Private Equity Index. Private debt: Pitchbook Private Debt Index. Private Real Estate: Pitchbook Private Real Estate Index. Hedge fund: HFRI Fund Weighted Composite Index. Public equity: MSCI All-Country World Index. High-yield fixed income: Bloomberg U.S. Corporate High Yield Index. Public Real Estate: FTSE NAREIT All Equity REITs Index. See back of report for index definitions. An index is unmanaged and not available for direct investment. **Past performance is no guarantee of future results.**

© 2024 Wells Fargo Investment Institute. All rights reserved.

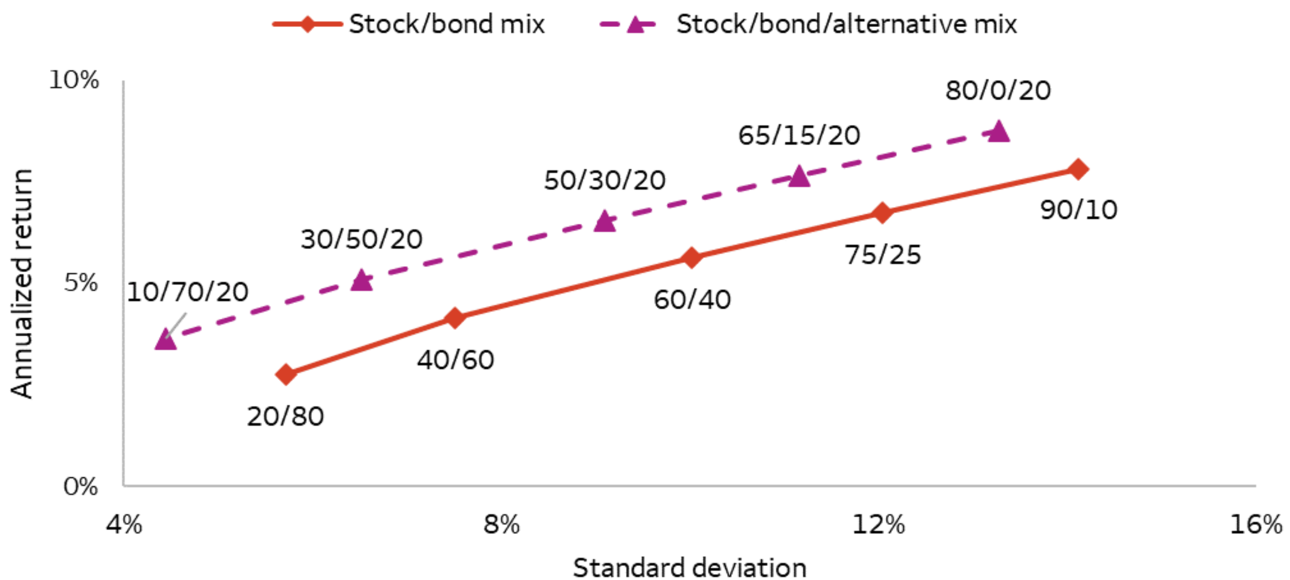
Given these potential benefits, our illiquid strategic allocation designed for qualified investors allocates 10% to 25% to alternatives. Over the 10-year period ending September 30, 2023, adding 20% alternative investments to a blend of stocks and bonds resulted in more favorable portfolio risks and returns (chart 2).

Another driver that has fueled the growth of alternatives is innovation. New strategies and products have been developed through the years to satisfy the needs of private businesses and investors alike.

- New strategy trends: Direct lending witnessed rapid growth in recent years, as private lenders provided desired financing certainty and speed. Direct lending also helped fill the financing gap created by banks' withdrawal from lending to many private companies due to regulatory and business reasons. Secondaries is another growing strategy that offers much-needed liquidity in private markets, where liquidity has been constrained by macro uncertainties and soft exit activities. Finally, infrastructure funds gained renewed interests, driven by policy supports and the need to electrify and digitize our society.
- Semi-liquid products: A new breed of products are increasingly available across private capital asset classes. Unlike traditional drawdown structures, these semi-liquid funds offer greater accessibility and allow periodic liquidity, immediate capital deployment, simplified tax reporting, and a potential lower investment minimum. According to Preqin, there are over 500 semi-liquid funds available globally, representing at least $350 billion in assets. Many products are tailored to high-net-worth investors.

We consider alternatives long-term investments, which can help improve investors' return and risk experience and increase the probability of achieving financial goals. To invest in alternatives, qualified investors should develop a diversified allocation based on liquidity need, time horizon consideration, and product vehicle preference.

Chart 2. Historical portfolio return and risk standard deviation with and without alternative investments



Sources: Wells Fargo Investment Institute, Pitchbook, and Bloomberg. Data as of September 30, 2023. Average annualized returns depicted are calculated over a 10-year period spanning fourth quarter (Q4) 2013 to Q3 2023. The figures along the lines represent the respective weights of the stock/bond or stock/bond/alternative mix. The 20% alternatives added are equally distributed across the four alternative asset classes, specifically 5% in private equity, 5% in private debt, 5% in private real estate, and 5% in hedge funds.

Private equities: Pitchbook Private Equity Index. Private debt: Pitchbook Private Debt Index. Private real estate: Pitchbook Private Real Estate Index. Hedge fund: HFRI Fund Weighted Composite Index. Public equity: MSCI All-Country World Index. High-yield fixed income: Bloomberg U.S. Corporate High Yield Index. Public real estate: FTSE NAREIT All-Equity REITs Index. An index is unmanaged and not available for direct investment.

© 2024 Wells Fargo Investment Institute. All rights reserved.

Equities

"For all your days prepare, and meet them ever alike." — Edwin Markham

Austin Pickle, CFA
Investment Strategy Analyst

Target change recap

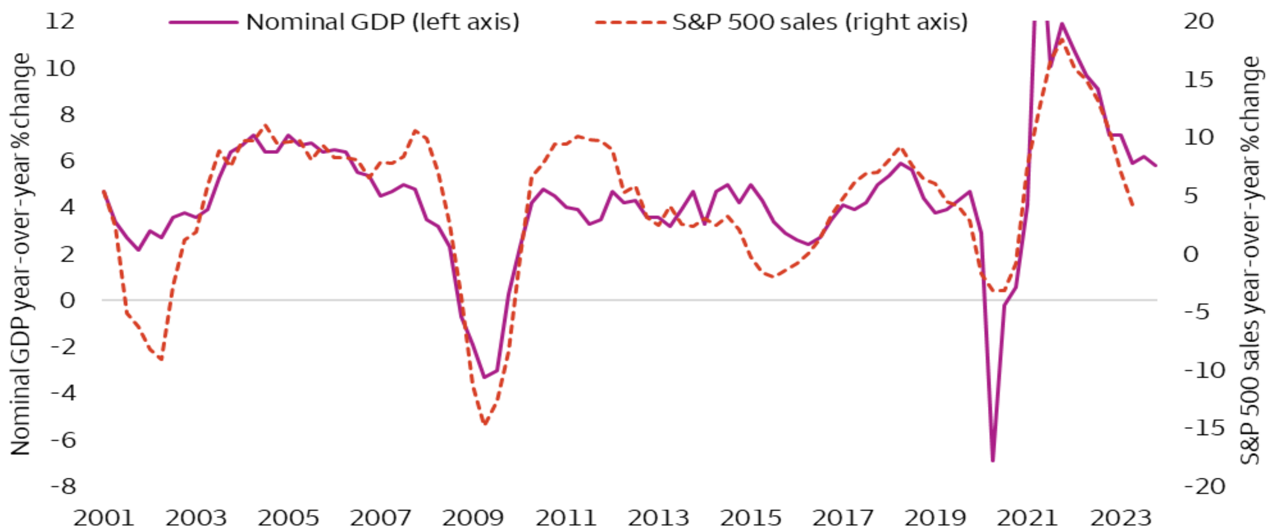
We introduced our 2025 equity earnings and price targets while simultaneously raising some of our 2024 targets in response to our improved economic outlook. We summarize the updates below.

For S&P 500 Index constituents, we believe supply chain issues are mostly in the rearview mirror; wage increases are moderating; labor efficiency (that is, sales per employee) is at an all-time high and may trend higher; and interest costs appear manageable. We believe positive economic growth should drive sales (see chart) while cost control should help anchor company profit margins. We expect S&P 500 Index earnings per share (EPS) to improve from $240 in 2024 to $260 in 2025.

Equity markets may have already priced in much of 2024's good news, however. We suspect that markets may struggle to advance meaningfully past recent highs while uncertainties persist surrounding the path of inflation, as well as the timing and magnitude of Fed rate cuts. Still, we would view periods of equity market weakness as opportunities, given that our outlook through 2025 supports improved revenue growth and expanding margins. We project the S&P 500 Index will likely end 2024 between 5100 and 5300 before resuming the trend higher to end 2025 between 5600 and 5800.

We continue to prefer a quality-based approach to portfolio positioning and remain favorable U.S. Large Cap Equities, as we view the group as the highest-quality major equity asset class due to strong company balance sheets, durable pricing power, and resilient growth potential. We believe these characteristics should help U.S. Large Cap Equities manage disappointments to sentiment more effectively than other domestic and international asset classes.

Higher GDP has generally translated into higher sales growth



Sources: Bloomberg and Wells Fargo Investment Institute. Quarterly data: March 31, 2001 – December 31, 2023. The trailing 12-month S&P 500 Index sales data is moved back 6 months. GDP = gross domestic product. Nominal GDP axis truncated at 12%. An index is unmanaged and not available for direct investment. **Past performance is no guarantee of future results.**

© 2024 Wells Fargo Investment Institute. All rights reserved.

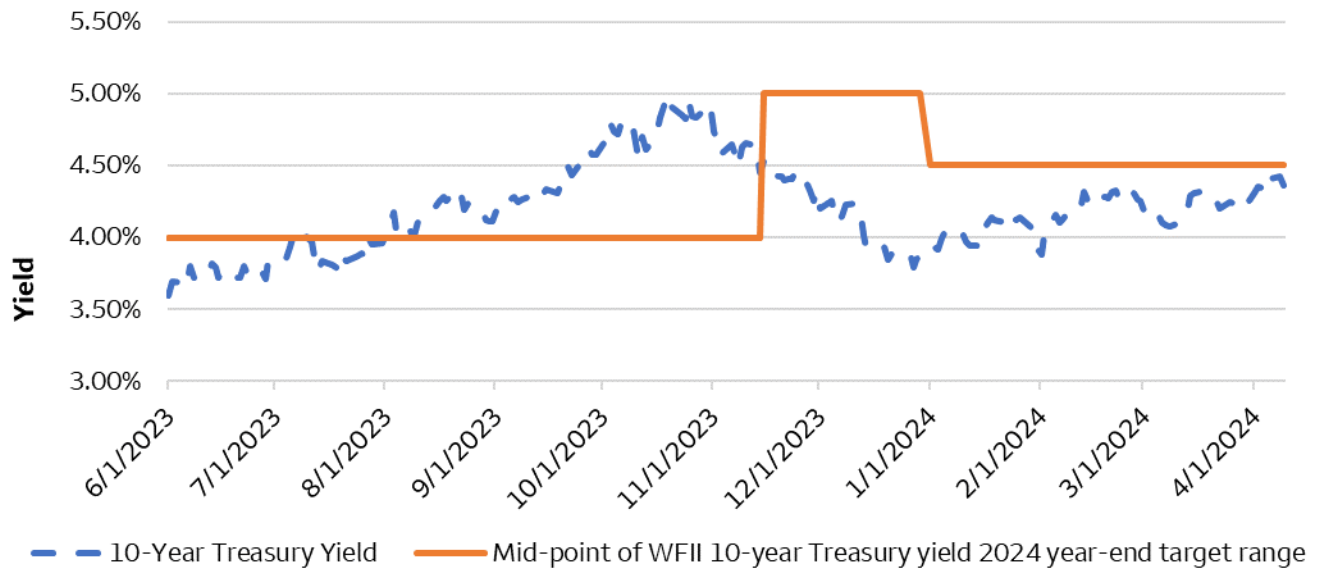
Fixed Income

Brian Rehling, CFA
Head of Global Fixed Income Strategy

10-year yields — A look back

10-year U.S. Treasury yields have experienced significant volatility since we first established a year-end 2024 target over 16 months ago. In our view there are three clear and distinct periods over this timeframe.

10-Year Treasury Yield



Sources: Wells Fargo Investment Institute (WFII) and Bloomberg, as of April 9, 2024.

- The Fed last increased the short-term federal funds rate on July 26, 2023, yet 10-year Treasury yields continued to trend higher through mid-October 2023 as inflation proved more stubborn to bring down than most market participants had expected.
- Falling inflation, weakening economic data, and concerns the Fed had gone too far began to emerge in the fall of 2023, and by the end of the year, markets were expecting six to seven 0.25% Fed rate cuts in 2024. During this period, 10-year Treasury yields fell dramatically from almost 5.00% to a low of 3.80% near year-end 2023.
- Year-to-date, 10-year Treasury yields have been on an upward trajectory as the economy has proven more resilient than most market participants have expected, and inflation has continued to run above Fed targets. We believe the market now expects just two or three Fed rate cuts this year. We just reduced our expectation from three Fed rate cuts in 2024 to two, and if the economy continues to remain resilient, we would not be surprised if the Fed leaves rates unchanged through year-end.

Until we see more evidence of economic slowing and moderating inflation, we believe that the near-term trend for longer-term rates is biased higher. 10-year Treasury yields are near the mid-point of our year-end target last week and a re-test of the October 2023 highs cannot be ruled out. We remain convicted that the Fed will eventually be successful in lowering inflation closer to its stated 2% goal, and we view levels near or above the upper-end of our 2024 target range of 4.25% – 4.75% as attractive levels to term out rate exposure.

© 2024 Wells Fargo Investment Institute. All rights reserved.

Real Assets

Mason Mendez
Investment Strategy Analyst

John LaForge
Head of Real Asset Strategy

Gold hitting new all-time highs – Raising targets

Gold did it again last week, on April 9, closing at another new all-time high. We say "again" because last week's new high, at $2353 per troy ounce, marked the 16th time this year that gold has closed at a new all-time high. Not surprisingly, its 14% return so far in 2024 has handily outpaced the 5.7% return of the broader Bloomberg Commodity Index (BCOM).

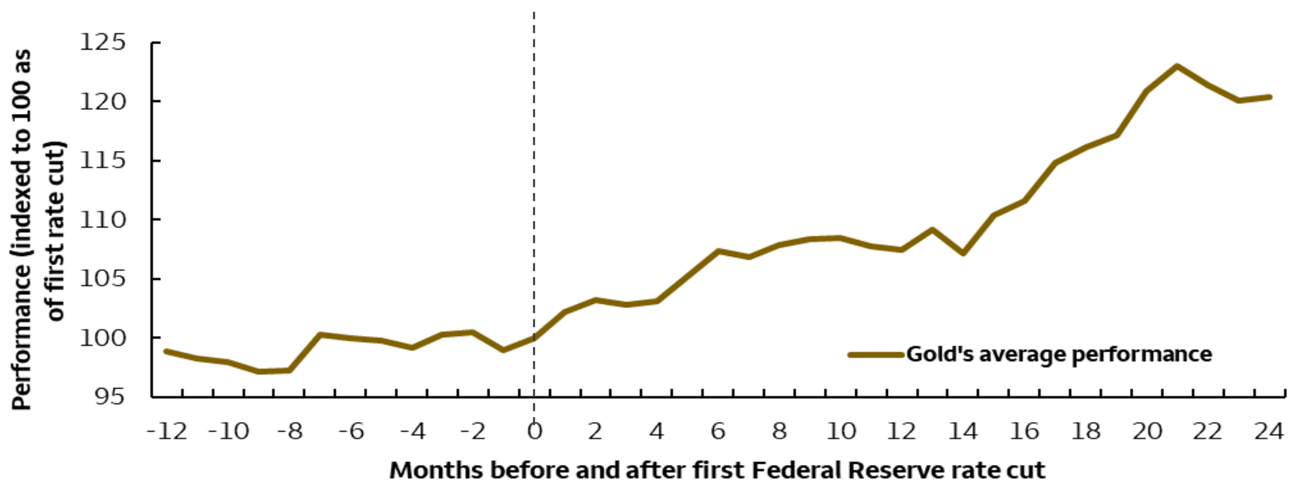
We believe gold owes its stellar start to the year to both technical and fundamental reasons. On the technical front, a string of new all-time highs by an asset is often viewed positively by investors. When the series of new all-time highs is accompanied by strong trading volumes, it can be especially attractive to long-term investors. The reason is that it often signals broad investor recognition that fundamental trends are strong, and the future looks bright. From what we see today, gold appears to have both strong fundamental trends and a bright future.

In our view, the main positive fundamental trends driving gold prices today are: 1) persistent purchases from global central banks, 2) growing demand from emerging market consumers, 3) stagnating supply growth, and 4) heightened geopolitical tensions. We do not anticipate these trends changing anytime soon.

As for gold's future over the next 6 to 18 months, we believe the shifting interest rate landscape could be a particularly powerful tailwind. While it is no secret that the Fed wants to cut interest rates later this year (if economic data permits), not as well-known is the fact that some of gold's strongest past performances have come during Fed rate-cut cycles. The chart shows the price of gold rising 20%, on average, in the 24 months following the start of Fed rate-cut cycles. Of course, past performance is not a guarantee of future results.

The bottom line is that we have been favorable on gold since 2022, so it is encouraging to see prices finally reflecting fundamentals. For this reason, we raised our 2024 forecast to $2,300 – $2,400 per troy ounce, and even higher to $2,400 — $2,500 per troy ounce for 2025. Worth noting is that we suspect gold may need to take a breather before it moves higher through 2025. Gold's 14% gain so far in 2024, as of April 9, is its best start to a year since 2012.

Gold's performance around Federal Reserve easing cycles



Sources: Bloomberg, Ned Davis Research, and Wells Fargo Investment Institute. Monthly data is from November 1969 – June 2021. The gold spot price (XAU) was used to measure performance. **Past performance is no guarantee of future results.**

© 2024 Wells Fargo Investment Institute. All rights reserved.

Tactical guidance*

Cash Alternatives and Fixed Income

Most Unfavorable	Unfavorable	Neutral	Favorable	Most Favorable
	High Yield Taxable Fixed Income	Cash Alternatives Developed Market Ex-U.S. Fixed Income Emerging Market Fixed Income U.S. Long Term Taxable Fixed Income U.S. Intermediate Term Taxable Fixed Income	U.S. Taxable Investment Grade Fixed Income	U.S. Short Term Taxable Fixed Income

Equities

Most Unfavorable	Unfavorable	Neutral	Favorable	Most Favorable
U.S. Small Cap Equities	Emerging Market Equities	U.S. Mid Cap Equities Developed Market Ex-U.S. Equities	U.S. Large Cap Equities	

Real Assets

Most Unfavorable	Unfavorable	Neutral	Favorable	Most Favorable
		Private Real Estate	Commodities	

Alternative Investments**

Most Unfavorable	Unfavorable	Neutral	Favorable	Most Favorable
		Hedge Funds—Event Driven Hedge Funds—Equity Hedge Private Equity Private Debt	Hedge Funds—Relative Value Hedge Funds—Macro	

Source: Wells Fargo Investment Institute, April 15, 2024.

*Tactical horizon is 6-18 months

**Alternative investments are not appropriate for all investors. They are speculative and involve a high degree of risk that is appropriate only for those investors who have the financial sophistication and expertise to evaluate the merits and risks of an investment in a fund and for which the fund does not represent a complete investment program. Please see end of report for important definitions and disclosures.

© 2024 Wells Fargo Investment Institute. All rights reserved.

Risk considerations

Each asset class has its own risk and return characteristics. The level of risk associated with a particular investment or asset class generally correlates with the level of return the investment or asset class might achieve. **Stock markets**, especially foreign markets, are volatile. Stock values may fluctuate in response to general economic and market conditions, the prospects of individual companies, and industry sectors. **Foreign investing** has additional risks including those associated with currency fluctuation, political and economic instability, and different accounting standards. These risks are heightened in emerging markets. **Small- and mid-cap stocks** are generally more volatile, subject to greater risks and are less liquid than large company stocks. **Bonds** are subject to market, interest rate, price, credit/default, liquidity, inflation and other risks. Prices tend to be inversely affected by changes in interest rates. **High yield (junk) bonds** have lower credit ratings and are subject to greater risk of default and greater principal risk. The **commodities** markets are considered speculative, carry substantial risks, and have experienced periods of extreme volatility. Investing in a volatile and uncertain commodities market may cause a portfolio to rapidly increase or decrease in value which may result in greater share price volatility. Investments in **gold** and gold-related investments tend to be more volatile than investments in traditional equity or debt securities. Such investments increase their vulnerability to international economic, monetary and political developments. **Real estate** has special risks including the possible illiquidity of underlying properties, credit risk, interest rate fluctuations and the impact of varied economic conditions.

Alternative investments, such as hedge funds, private equity/private debt and private real estate funds, are speculative and involve a high degree of risk that is appropriate only for those investors who have the financial sophistication and expertise to evaluate the merits and risks of an investment in a fund and for which the fund does not represent a complete investment program. They entail significant risks that can include losses due to leveraging or other speculative investment practices, lack of liquidity, volatility of returns, restrictions on transferring interests in a fund, potential lack of diversification, absence and/or delay of information regarding valuations and pricing, complex tax structures and delays in tax reporting, less regulation and higher fees than mutual funds. Hedge fund, private equity, private debt and private real estate fund investing involves other material risks including capital loss and the loss of the entire amount invested. A fund's offering documents should be carefully reviewed prior to investing.

Hedge fund strategies, such as Equity Hedge, Event Driven, Macro and Relative Value, may expose investors to the risks associated with the use of short selling, leverage, derivatives and arbitrage methodologies. Short sales involve leverage and theoretically unlimited loss potential since the market price of securities sold short may continuously increase. The use of leverage in a portfolio varies by strategy. Leverage can significantly increase return potential but create greater risk of loss. Derivatives generally have implied leverage which can magnify volatility and may entail other risks such as market, interest rate, credit, counterparty and management risks. Arbitrage strategies expose a fund to the risk that the anticipated arbitrage opportunities will not develop as anticipated, resulting in potentially reduced returns or losses to the fund.

Definitions

Bloomberg Commodity Index is comprised of 22 exchange-traded futures on physical commodities and represents 20 commodities weighted to account for economic significance and market liquidity.

Bloomberg U.S. Corporate High Yield Index covers the universe of fixed-rate, noninvestment-grade debt.

FTSE NAREIT All Equity REITs Index is designed to represent all U.S. commercial real estate sectors and contains all tax-qualified REITs with more than 50% assets in real estate.

HFRI Fund Weighted Composite Index is a global, equal-weighted index of single-manager funds that report to HFR Database.

MSCI All Country World Index (MSCI ACWI) is a free float-adjusted market capitalization weighted index that is designed to measure the equity market performance of 23 developed and 26 emerging markets.

Pitchbook Private Debt Index is based on the pool of private debt closed end funds sourced by Pitchbook and is asset weighted.

Pitchbook Private Equity Index is based on the pool of private equity closed end funds sourced by Pitchbook and is asset weighted.

Pitchbook Private Real Estate Index is a quarterly return benchmark built with Pitchbook's fund cash flow and net asset value data. The index includes private real estate funds classified by Pitchbook. The index is capital weighted and provides estimates of asset class performance that are subject to updates by Pitchbook.

S&P 500 Index is a market capitalization-weighted index composed of 500 widely held common stocks that is generally considered representative of the US stock market.

An index is unmanaged and not available for direct investment.

General disclosures

Global Investment Strategy (GIS) is a division of Wells Fargo Investment Institute, Inc. (WFII). WFII is a registered investment adviser and wholly owned subsidiary of Wells Fargo Bank, N.A., a bank affiliate of Wells Fargo & Company.

The information in this report was prepared by Global Investment Strategy. Opinions represent GIS' opinion as of the date of this report and are for general information purposes only and are not intended to predict or guarantee the future performance of any individual security, market sector or the markets generally.

© 2024 Wells Fargo Investment Institute. All rights reserved.

GIS does not undertake to advise you of any change in its opinions or the information contained in this report. Wells Fargo & Company affiliates may issue reports or have opinions that are inconsistent with, and reach different conclusions from, this report.

The information contained herein constitutes general information and is not directed to, designed for, or individually tailored to, any particular investor or potential investor. This report is not intended to be a client-specific suitability or best interest analysis or recommendation, an offer to participate in any investment, or a recommendation to buy, hold or sell securities. Do not use this report as the sole basis for investment decisions. Do not select an asset class or investment product based on performance alone. Consider all relevant information, including your existing portfolio, investment objectives, risk tolerance, liquidity needs and investment time horizon. The material contained herein has been prepared from sources and data we believe to be reliable but we make no guarantee to its accuracy or completeness.

Wells Fargo Advisors is registered with the U.S. Securities and Exchange Commission and the Financial Industry Regulatory Authority, but is not licensed or registered with any financial services regulatory authority outside of the U.S. Non-U.S. residents who maintain U.S.-based financial services account(s) with Wells Fargo Advisors may not be afforded certain protections conferred by legislation and regulations in their country of residence in respect of any investments, investment transactions or communications made with Wells Fargo Advisors.

Wells Fargo Advisors is a trade name used by Wells Fargo Clearing Services, LLC and Wells Fargo Advisors Financial Network, LLC, Members SIPC, separate registered broker-dealers and non-bank affiliates of Wells Fargo & Company. PM-10112025-6546137.1.1

© 2024 Wells Fargo Investment Institute. All rights reserved.