Surfside Police Retirement Trust

Investment Review

Period Ending

December 31, 2024

Highland Capital MANAGEMENT, LLC

An Argent Company

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4Q24 Equity Commentary

In the fourth quarter of 2024 the market posted a solid gain of 2.39%, bringing the full year return to +25% for 2024, the first time for consecutive 20%+ years since 1997 – 98. The market experienced minimal pre-election jitters with the market declining roughly 1% in October, only to rebound in November post the election to gain 5.7% for the month. December closed on a down note with the traditional Santa Claus rally failing to materialize as the market declined 2.38%. The Mag 7 stocks were the market drivers in 2024, with the group accounting for 55% of the index return, and Nvidia alone accounting for roughly 21% of the markets return. The Mag 7 stocks are now almost 30% of the market capitalization of the S&P 500, and the top 10 stocks in the index now represent 38% - so much for diversification! The biggest events of the quarter were the election, followed by the Federal Reserve moving to a more hawkish stance in their December 18th release where they cut short terms rates by another 25 basis points, but also indicated they are "data dependent" going forward as inflation remains "somewhat elevated". The market interpreted the news as indicating that the Fed could pause rate cuts until more progress is made on inflation. In the Fed's Summary of Economic Projections, they raised their estimate of core PCE inflation to 2.5% in 2025 from 2.2% previously and lowered the number of estimated rate cuts in 2025 from 4 cuts to just two. However, we must also remember that the Fed has been wrong in their assessments of the economy for the past few years. Perhaps the Fed is hedging as they (like us), are unsure of what changes to anticipate from the incoming new administration. We view tariffs as being potentially inflationary, but at this point we don't know if tariffs are being used as a negotiating tool, or if not, what level of tariffs would be implemented. I doubt that anyone relishes a trade war, and globalization has made major world economies more reliant on each other, not less. GDP continued to grow at an above-trend rate with Q3 growth coming in 3.1%, making this the second consecutive quarter of 3%+ growth. The unemployment rate has moved up to 4.2%, and the labor market is showing some signs of loosening. The economy added 227,000 jobs in November, but just 36,000 in October. For 2024 monthly job growth has averaged 200,000 versus 250,000 in 2023. The jobs market could hold the key as what Fed actions take place in 2025. A weakening jobs market could cause the Fed to cut as they want to stay ahead of a precipitous decline in employment. In contrast, a stable jobs market coupled with sticky inflation could keep them on hold. Regardless, we would expect that volatility in 2025 will be higher as new policies, executive orders, tax legislation, and debt limits are considered.

The Economy: The US economy continues to outpace the rest of the world's major economies. Yes, we have overindulged by running deficits of almost 7%, but the US remains the world's leader in innovation and capital formation, which are vital to growth. Germany, France, and the UK have had growth of -0.1%, 1.1%, and 1% in 2024, and all are projected to be near 1 – 1.5% growth in 2025. US GDP is expected to slow to 2% in 2025, but this will again outpace other major economies. One of the questions for 2025 is whether the US can continue to grow while other major economies around the world remain relatively weak. China has begun to stimulate its economy on both the fiscal and monetary sides, and this is needed to bring the world's second-largest economy back on track. The World Bank sees China's growth at 4.9% in 2024 and 4.5% in 2025. And while China has moved to make their economy less dependent on the US, they will be in the cross hairs of trade policy in the Trump administration. But in our opinion, inflation will be the key to the US economy in 2025. Core PCE inflation for November came in at 2.8% and was 0.1% higher than October, while the headline number came in at 2.4%. The increase again came from services, which over the past 12 months have risen 3.8%, while goods prices have

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declined 0.4%. Shelter inflation peaked in April of 2023 at 8.3% but is still elevated at 4.8%. New administration policies and their implementation will be important to the inflation trajectory. Tariffs are inherently inflationary, but tariffs that are too harsh could slow growth and offset the inflationary tilt. An immigration policy which deports large numbers would tighten the labor market and add to wage pressures. Based on more realistic expectations, deportations are likely to be in the 300,000 to 500,000 range and represent 0.2% to 0.3% of the labor force. This could keep the unemployment rate in check and ease the Fed's concern on that front. On the plus side, deregulation could lower compliance costs for companies and improve productivity which would be an offset to possible inflation from tariffs and immigration policy. Suffice it to say that there any many nuances that will play against each other as these programs are rolled out, and both their timing and level of intensity will matter. Tax policy is likely to be more of an issue in later 2025, and how the deficit trends in 2025 along with interest rates and inflation could have an impact on what gets extended or changed in terms of both corporate and individual tax policies. Will fiscal spending finally be constrained with the efforts of the Department of Governmental Efficiency? We're not holding our breath on that one, but certainly hoping that a focus on reigning in wasteful expenditures can have some benefit.

Fourth Quarter Market Recap: The top performing sector in a down Q4 was Consumer Discretionary gaining 14.3% as the two largest weights in the category experienced a strong Q4. Tesla jumped after the election and tacked on 60% from November 5th through year end, finishing the quarter up 54.3%. Amazon added 17.7% during Q4 as online sales continued to be strong driven by a resilient consumer. Tesla and Amazon combined account for 38% of the weighting in the Discretionary sector. Communications Services gained 8.9% led by Alphabet, which advanced 14.2% driven by news of a breakthrough in their quantum computing chip. Financials also had a solid quarter, rising 7.1% as the sector is expected to be a beneficiary of lighter regulation that could free up capital for banks and result in more merger and acquisition activity. Materials lagged in Q4 and declined 12.4% as various global manufacturing indices were weaker than expected, China continued to remain depressed, and the sector is sensitive to higher interest rates. Healthcare also declined 10.3% in Q4, as GLP1 (weight loss stocks) lost ground and investors worried about potential new administration appointments that could result in price pressure for the group. Real Estate was down 7.9% as higher interest rates (mortgage rates) weighed on the group. In a sign of how bifurcated the market was in 2024, the S&P 500 return ex the Mag 7 stocks was just 10%, highlighting the concentrated nature of the market and the impact of the AI boom. For all of 2024 Communications Services was the best performing sector at +40%, with Meta gaining 66% and Google 36%. Meta has already been an AI beneficiary as AI has helped them to optimize advertising spend for companies and effectively target customers. Technology was the second top performer in 2024 at +36.6%, with Nvidia again leading with an eye-popping gain of 171%. There were other strong chip stocks in the year as well, with Broadcom gaining 110%. Sectors that lagged in 2024 were Materials (0%), Healthcare (+2.6%), and Real Estate (+5.2%).

What to Expect Going Forward: The economic underpinnings entering 2025 appear to be solid, but we anticipate greater volatility in the new year as executive orders and trade policy come to light. With two very strong years of equity returns in the rear-view mirror, it's only prudent to moderate expectations for returns in the future. In our favor for 2025 is that returns in the first year of a new Presidential cycle have averaged +7.4% going all the way back to 1933 with the caveat that the economy doesn't go into recession. We view the odds of a recession as low. Another positive for the

4Q24 Equity Commentary

new year is that there should be a liquidity infusion of roughly $400 billion in Q1 because of the debt ceiling impasse which forces the Treasury to spend down their $700 billion General Account. This moves money into the banking system and loosens financial conditions which should in the short term bring down bond yields and the US dollar. When starting with market valuations that are historically elevated on almost every measure, we view the need for corporate earnings to hit their mark in 2025 as of paramount importance. We would not expect to see multiple expansion in 2025, especially if the rate cutting cycle is muted due to inflation running above the Fed’s target. After earnings gains of roughly 9% in 2024, consensus expects earnings to grow by almost 15% in 2025. That will require a broadening of earnings growth across more sectors that are not technology centric. The US dollar remains high after rising almost 7% in 2024. A stronger dollar is a headwind for large companies that receive a big percentage of their revenues from outside the US, and we have already mentioned that other developed economies are not exactly in growth mode. This could have a dampening impact on earnings. While lower rates from the Fed should help, we recognize that support is clearly diminished since the last Fed meeting. The market is trading at 21.5X forward earnings, and the multiple of the top 10 stocks by market capitalization is 29.8X, while the remaining 490 stocks are selling at a more reasonable 18.2X multiple. There is still a large valuation gap between growth and value stocks, with Growth stocks trading at 28.9X, and Value at 16.2X. With the level of market concentration currently, if the Mag 7 stocks lag it will be hard for the index to show gains, yet the remaining 493 stocks could perform better as investment dollars reallocate and the market performance broadens. The uptake on AI adoption by companies and its hopeful productivity improvements could be a boost to growth and profitability. However, the bill on massive AI spending to build out data center infrastructure at Microsoft, Amazon, Google, and Meta could be coming due. To earn their traditional 50% gross margins on estimated $250 billion of data center spending it means that they will need $400 - $500 billion of new revenues to maintain those margins. That is no small feat, and companies will need to see a tangible benefit to start purchasing AI applications, otherwise we could start to see earnings pressured at those companies. There are still geopolitical risks at play, and we can hope that a cessation of tensions can lead to a “peace dividend”. It will certainly be an interesting year with lots of moving pieces to keep investors on their toes.

We wish you a healthy and prosperous New Year, and as always, feel free to contact us if you have any questions regarding your portfolios.

4Q24 Fixed Income Commentary

As 2024 concluded, the Federal Reserve adopted a hawkish stance, indicating that it was a “close call” in deciding to lower short term borrowing costs. Despite a reduction in the benchmark rate and the Reverse Repo Program adjustment, the Federal Reserve forecasts only two rate cuts in 2025, raising the terminal rate to 3%. Diverging opinions within the Federal Open Market Committee (FOMC) signal less consensus, increasing the likelihood of prolonged higher rates. Additionally, the Federal Reserve upgraded its core PCE inflation projection for 2025 to 2.5%, underscoring persistent inflationary pressures.

The Fed’s interest rate hikes since March 2022 have not significantly slowed the U.S. economy, contrary to historical patterns and market consensus as the hiking cycle started. Typically, tighter monetary policy impacts the economy within 12-18 months, yet 30 months into this cycle, key economic indicators such as home sales, car purchases, and capital expenditures remain resilient. This resilience stems from structural factors, including low mortgage sensitivity—95% of U.S. mortgages are fixed-rate—and policy initiatives like the CHIPS Act and Inflation Reduction Act, which have spurred construction and domestic manufacturing.

Despite these challenges, the U.S. economy’s strength has created a supportive environment for consumers and corporations. Household debt-to-income ratios remain favorable compared to other economies, and firms have largely weathered rate hikes. However, the expanding federal debt, which surpassed $36 trillion in 2024, poses risks. Interest payments on the debt reached $870 billion, exceeding defense spending for the first time. This trend is projected to worsen, with $7.6 trillion in interest-bearing debt maturing in 2025. Such pressures could sustain higher long-term interest rates due to a supply-demand imbalance.

The bond market’s performance in the fourth quarter was influenced by evolving Fed policies, concerns over persistent inflation and a stubborn US consumer. At a high level, the best performing bond investments in 2024 were short duration in nature and contained as much risk as possible. The Bloomberg Aggregate (+1.25%), lagged both the Bloomberg Intermediate Gov/Credit (+3.0%) and the Bloomberg US Gov 1-3 year index (+4.04%). Long dated Treasuries (-8.82%) were a notable outlier, as the yield curve steepened. Over the past decade, diversification has been less effective for equity portfolios but has remained a critical strategy for bond investors. The bond market's diversity, spanning government-issued securities to esoteric asset-backed securities, has provided investors with opportunities amidst volatility. Notably, the regional banking crisis created a unique opening to acquire AAA-rated bonds, such as Agency CMBS and Agency MBS, at spreads nearly double historical levels. This supply-demand imbalance enabled purchases of risk-free assets with attractive returns.

Looking ahead, bond investors face a complex environment. The Fed’s slower-than-expected pace of rate cuts reflects the U.S. economy’s pronounced resilience, supported by policy-driven growth and strong household balance sheets. However, rising government debt and escalating interest payments present long-term risks to fiscal stability, potentially driving yields higher. With GDP growth forecasted at 2.5% for 2024 and core PCE inflation trending toward the Fed’s 2% goal, the U.S. economy appears well-positioned to navigate these challenges. Yet, the sustained fiscal deficits and Treasury issuance will remain critical factors influencing the bond market.

4Q24 Fixed Income Portfolio Manager Commentary

In conclusion, bond investors must navigate a landscape shaped by persistent inflation, slower monetary easing, and growing fiscal pressures. Opportunities exist but careful positioning will be crucial to managing the risks associated with higher-for-longer interest rates and fiscal imbalances. We continue to favor assets that produce a steady stream of cash flow to help dampen ongoing volatility, produce superior incremental yield and are backed by high quality collateral should the economy face unforeseen economic challenges in 2025.

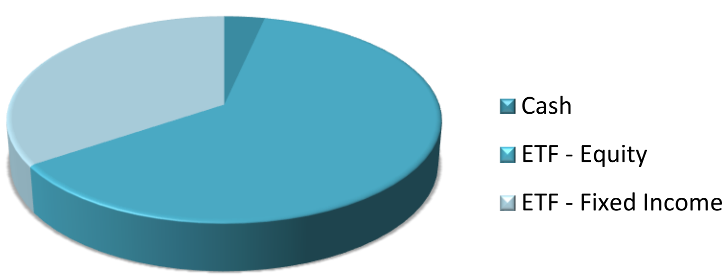
Surfside Police Retirement Trust **Period Ending 12/31/2024**

Total Return Summary

	Beginning Market Value	Ending Market Value	Difference	Contributions	Withdrawals	Gain/Loss	Cumulative Return	Annualized Return
Quarter (10/1/24 - 12/31/24)	$930,771	$871,233	-$59,538	$0	-$53,428	-$6,109	**-0.70%**	-------
One Year (1/1/24 - 12/31/24)	$863,214	$871,233	$8,019	$1,353	-$85,637	$92,303	**10.89%**	-------
Five Year (1/1/20 - 12/31/24)	$758,552	$871,233	$112,682	$258,527	-$434,510	$288,665	**39.70%**	**6.92%**

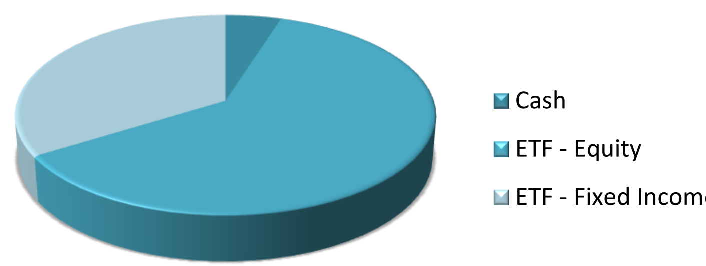
Asset Allocation

As of 9/30/2024



Cash	$32,211	3.5%
ETF - Equity	$578,629	62.2%
ETF - Fixed Income	$319,930	34.4%
Total	**$930,771**	**100.0%**

As of 12/31/2024



Cash	$42,766	4.9%
ETF - Equity	$533,907	61.3%
ETF - Fixed Income	$294,561	33.8%
Total	**$871,233**	**100.0%**

Portfolio Holdings

Quantity	Security	Unit Cost	Total Cost	Price	Market Value	Pct. Assets	Cur. Yield	Moody's Ratings	Coupon %	Maturity Date
CASH AND EQUIVALENTS (USD)										
	CASH		24,311.45		24,311.45	2.8	4.3			
	SCHWAB GOVERNMENT MONEY FUND		18,454.27		18,454.27	2.1	4.1			
			42,765.72		**42,765.72**	**4.9**	**4.2**			
ETF - EQUITY (USD)										
	Equitys ETF									
642	iSHARES CORE MSCI EMERGING MARKETS	63.86	40,997.48	52.22	33,525.24	3.8	3.2			
1026	iSHARES MSCI ACWI INDEX FUND	42.06	43,157.28	52.16	53,516.16	6.1	3.0			
291	iSHARES RUSSELL 1000 ETF	114.98	33,459.34	322.16	93,748.56	10.8	1.1			
160	RUSSELL 1000 GROWTH INDEX	262.86	42,057.60	401.58	64,252.80	7.4	0.5			
280	RUSSELL 1000 VALUE INDEX	163.21	45,698.13	185.13	51,836.40	5.9	1.9			
600	RUSSELL MIDCAP INDEX	75.67	45,399.36	88.40	53,040.00	6.1	1.3			
464	VANGUARD MID CAP VALUE INDEX FUND	121.84	56,533.71	161.77	75,061.28	8.6	2.1			
200	VANGUARD SMALL CAP GROWTH ETF	236.21	47,241.62	280.06	56,012.00	6.4	0.5			
267	VANGUARD SMALL CAP VALUE	148.67	39,696.22	198.18	52,914.06	6.1	2.0			
			394,240.75		**533,906.50**	**61.3**	**1.6**			
			394,240.75		**533,906.50**	**61.3**	**1.6**			
ETF - Fixed Income (USD)										
	Bonds ETF									
720	iSHARES BARCLAYS INT GOV/CRED BOND FND	102.80	74,013.48	104.23	75,045.60	8.6	3.4			
483	iSHARES BARCLAYS MBS BOND FUND	103.04	49,766.15	91.68	44,281.44	5.1	3.9			
924	iSHARES CORE US AGGREGATE BOND	111.58	103,102.22	96.90	89,535.60	10.3	3.7			
2870	SPDR PORTFOLIO SHORT TERM COR	30.26	86,855.23	29.86	85,698.20	9.8	4.8			
			313,737.08		**294,560.84**	**33.8**	**4.0**			
			313,737.08		**294,560.84**	**33.8**	**4.0**			
			750,743.55		**871,233.06**	**100.0**	**2.5**			
TOTAL PORTFOLIO			**750,743.55**		**871,233.06**	**100.0**	**2.5**			

Sales

Trade Date	Settle Date	Quantity	Security	Unit Price	Amount	Comm/ Share	Commission
schwab							
11/7/24	11/8/24	150.00	iSHARES BARCLAYS INT GOV/CRED BOND	104.84	15,726.17	0.00	0.00
11/7/24	11/8/24	380.00	iSHARES MSCI ACWI INDEX FUND	55.54	21,104.59	0.00	0.00
11/7/24	11/8/24	60.00	iSHARES RUSSELL 1000 ETF	327.11	19,626.64	0.00	0.00
					56,457.40	**0.00**	**0.00**
SALES SUBTOTAL					**56,457.40**	**0.00**	**0.00**
						0.00	**0.00**
TOTAL PORTFOLIO						**0.00**	**0.00**

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