GLOBAL
Insight

RBC Wealth Management

Perspectives from the Global Portfolio Advisory Committee

January 2025

Trend & Cycle 2025 Technical Outlook

Studying trends and cycles can provide a more informed view of market dynamics. We look at potential pause points, market breadth, and key interest rate levels to gauge prospects for equity upside in 2025 and how to approach sector positioning.

Robert Sluymer, CFA | Page 4

Also in this issue

GLOBAL EQUITY

Benefit of the doubt

GLOBAL FIXED INCOME

The Fed at risk of a missed approach?

U.S. RECESSION SCORECARD

New year, same Scorecard

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For important and required non-U.S. analyst disclosures, see page 19.

GLOBAL

Insight

January 2025

Contents

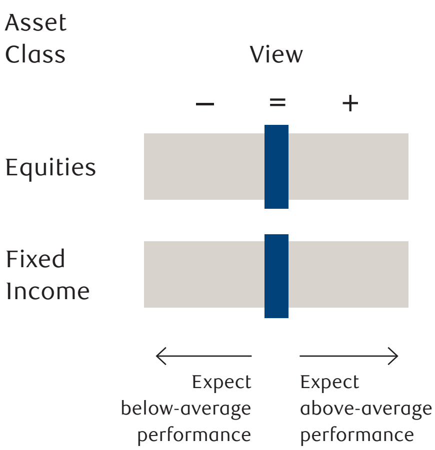
In the markets

All values in U.S. dollars and priced as of market close, Dec. 31, 2024, unless otherwise stated.

Wealth Management

RBC'S INVESTMENT
Stance

Global asset class views



(+/=/–) represents the Global Portfolio Advisory Committee's (GPAC) view over a 12-month investment time horizon.

+ Overweight implies the potential for better-than-average performance for the asset class or for the region relative to other asset classes or regions.

= Market Weight implies the potential for average performance for the asset class or for the region relative to other asset classes or regions.

– Underweight implies the potential for below-average performance for the asset class or for the region relative to other asset classes or regions.

Source - RBC Wealth Management

Equities

- In 2025, global equity markets have the potential to add to the strong gains of the past two years. We believe this would require economic and earnings growth that don't falter.
- In addition to the pro-growth tax and regulatory policies of the incoming Trump administration, markets may need to contend with the most aggressive tariff policies in almost 100 years. This makes central banks' job of forecasting inflation and GDP growth, and properly calibrating interest rates, more complex. Although moves out of Washington are rarely the sole determinant of the fate of the U.S. and other major economies, global markets will pay closer attention to U.S. policies this year, which could generate both volatility and opportunities.
- At this stage, RBC Capital Markets anticipates mid-single-digit gains for the S&P 500 in 2025. Already-stretched valuations and increasingly frothy investor sentiment readings argue to us that the appropriate positioning for the year ahead in a global balanced portfolio would have equities at, but not above, the long-term target exposure. We recommend an approach that is "watchful, cautious, but invested."

Fixed income

- Global bond yields remained largely steady in Q4 2024, with the average yield on the Bloomberg Global Aggregate ex-USD Index hovering around 2.6%. The same can't be said for U.S. yields, where the average yield on the Bloomberg U.S. Aggregate Bond Index jumped to nearly 5.0% from a low of 4.2% at the start of October. A hawkish Fed meeting in December, with policymakers seeing far fewer rate cuts in 2025 on renewed inflation risks, drove the move, while global central banks appear to remain largely on track to proceed with policy rate easing this year.
- In the U.S., we reduced our position in U.S. Treasuries in early December to Underweight from Overweight on the expectation that the Fed could cut rates less than global central banks. As a result, we increased our global developed market bond allocation to Market Weight from Underweight.
- We reiterate our Market Weight stance on U.S. fixed income with yields remaining above multi-decade averages. Globally, we favor sovereign bonds over corporate bonds as we think valuations in the latter remain historically rich.

MONTHLY

Focus

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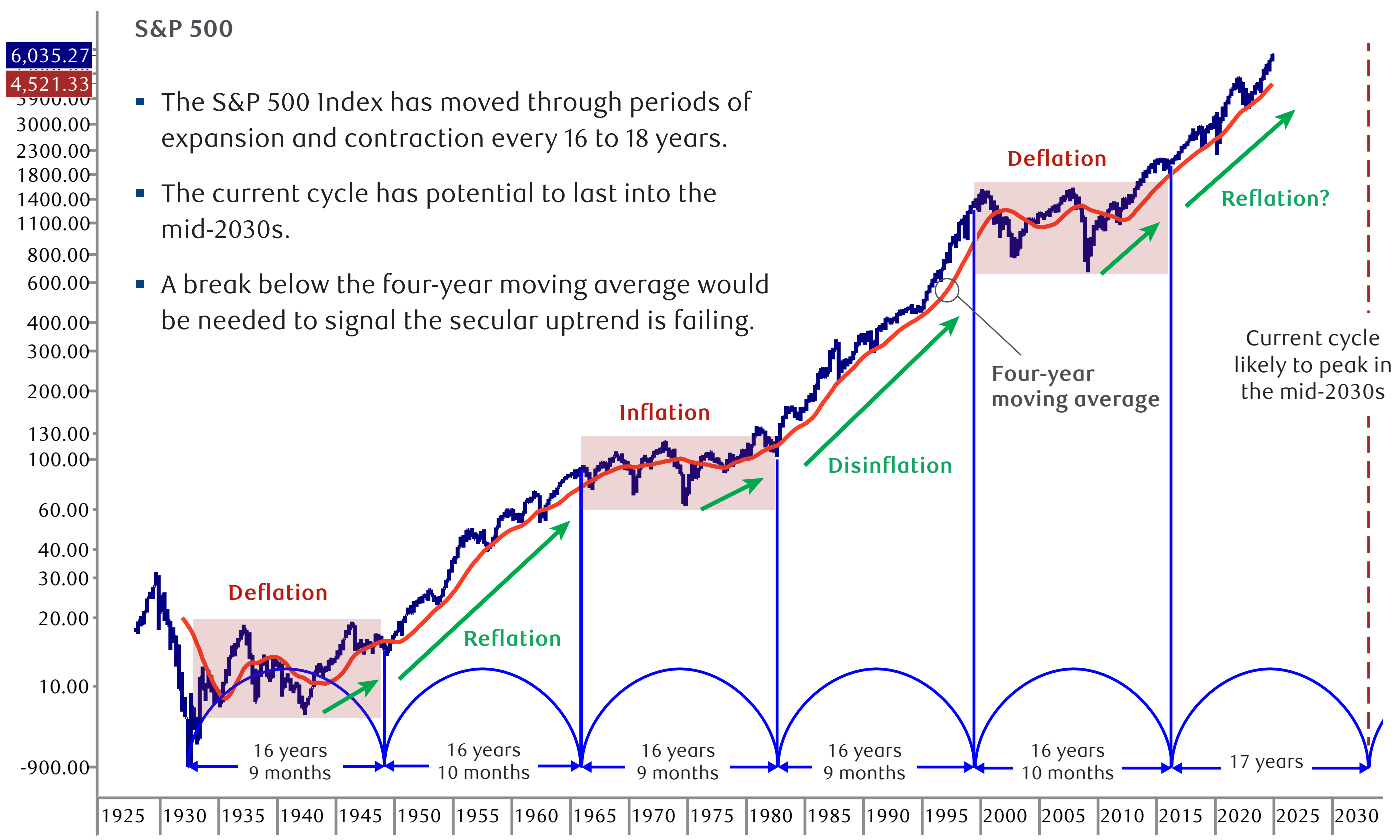
Trend & Cycle 2025 Technical Outlook

The following is a summary of our Technical Outlook published in December. We believe our approach provides an important perspective by studying the market's trends and cycles using technical analysis. The combination of both a macro-fundamental and technical approach can identify where the two agree and/or disagree, providing a more informed view of market dynamics for investors.

At the beginning of each year, investors often step back to assess the risks and opportunities that may develop in the year ahead based on their expectations for corporate profitability underpinned by the prospects for economic growth, inflation, interest rates, government policy, geopolitics, etc. Combining this "macro" view with our technical approach can provide a helpful context for making investment decisions.

The chart below illustrates that the U.S. equity market moves through expansion and contraction/consolidation cycles lasting roughly 16–18 years. Looked at this way, we see potential for the current cycle to last into the mid-2030s before another extended period of sideways consolidation develops. While multi-quarter pullbacks often develop along the way, the takeaway is to stay invested in the current longer-term uptrend.



Source - RBC Wealth Management, Bloomberg, Optuma

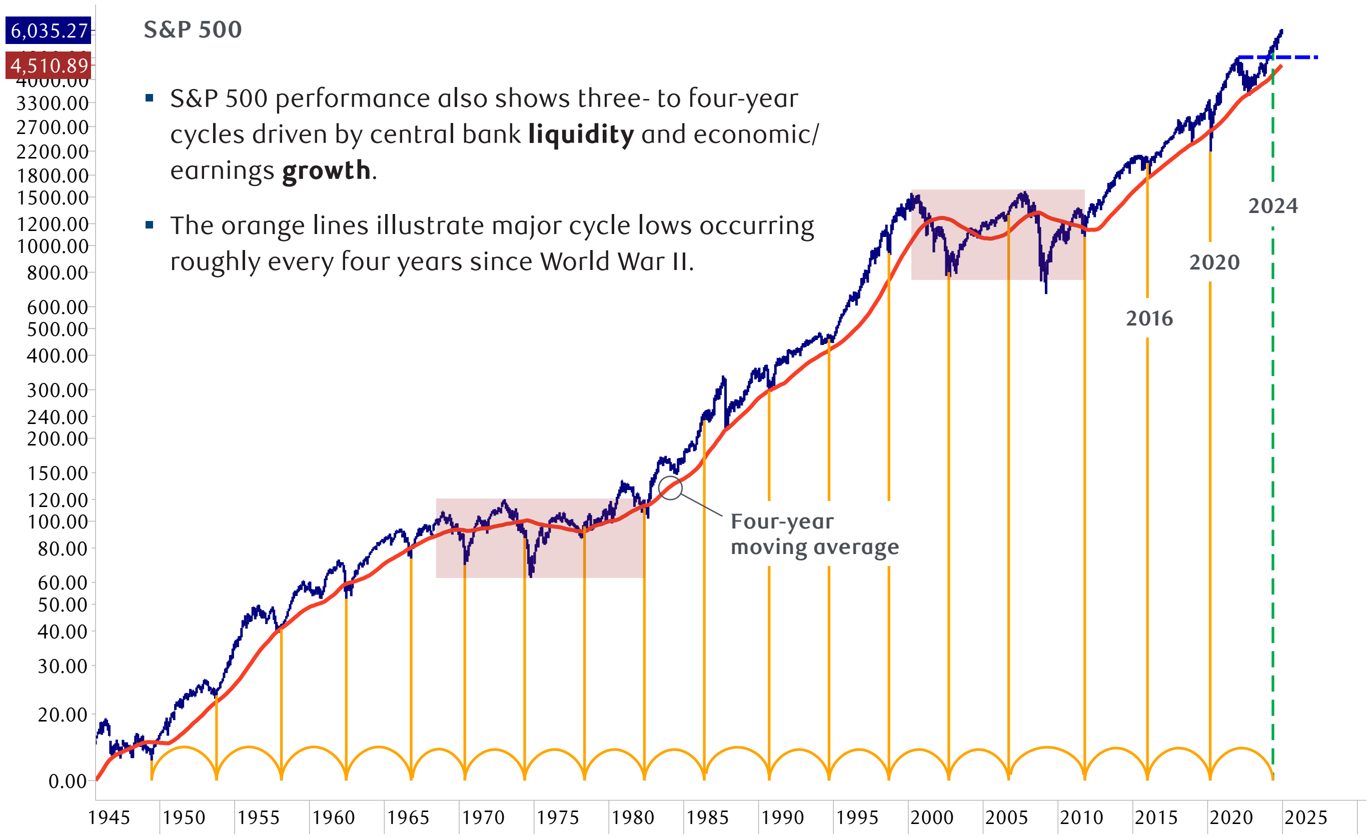
TREND & CYCLE
2025 TECHNICAL OUTLOOK

Bull market cycles

The structural bull markets of the 1950s–1960s, 1980s–1990s, and 2010s–2020s are made up of smaller stair-step cycles that bottom roughly every four years, often near a rising four-year moving average. These four-year cycles are by no means symmetrical, with some cycles extending beyond the usual two- to three-year rallies followed by a 9- to 12-month correction, of which 1987 and 2007 are two examples.

What drives these cycles? Liquidity provided by central banks and the response to that liquidity by the economy and corporate earnings are the primary catalysts, in our view. Although returns vary significantly for each four-year cycle, during structural bull markets the average four-year cycle upside has been near 110%, while the average decline has been 23%. Interestingly, the 2020–2021 bull market (+120%) and 2022 bear market (-27%) line up with the historical averages.

We think the implication for the current cycle that bottomed in Q4 2022 is that equities should see further upside in 2025 with a corrective window likely in 2026. The current four-year upcycle bottomed in Q4 2022 at the rising red four-year moving average, and after breaking out to new highs in early 2024, it remains in an uptrend (see chart below).



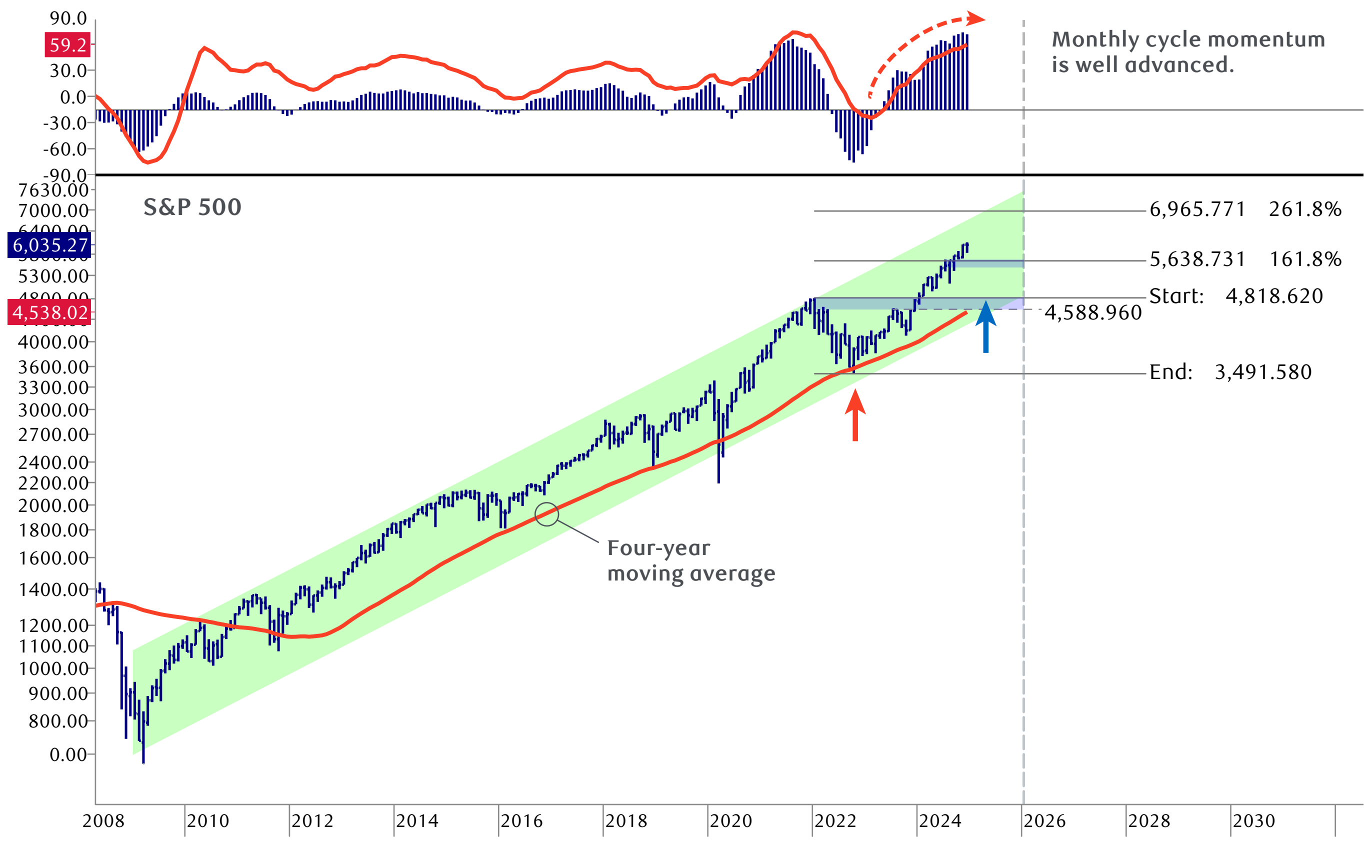
Source - RBC Wealth Management, Bloomberg, Optuma

TREND & CYCLE
2025 TECHNICAL OUTLOOK

Pause points

Once a market or security moves to new highs, one technical method to identify potential upside pause points is to take the prior trading range, in this case the 2022–2024 range, and multiply it by 1.618 and 2.618 (both derived from the Golden Mean). We appreciate this may seem like an odd way to forecast potential upside levels, but we are impressed by how often markets inflect near these arithmetic markers. Interestingly, the first 161.8% extension was where the S&P 500 and Nasdaq 100 Indexes stalled in July. While we expect a volatile H1 2025, the next upside level for the S&P 500 is near 7000 at the 261.8% extension level.

While this suggests to us further upside in 2025, after a two-year rally, the cycle may be at risk of maturing. The momentum indicator in the top panel of the chart has proven useful to track prior three- to four-year market cycles. After bottoming in Q4 2022, that indicator transitioned into overbought territory and could be at risk of turning negative in 2025. What could cause the current equity cycle to peak? Higher bond yields are often the culprit. While our expectation is for the U.S. 10-year yield to trade in a band between 3.25% and 5%, a move above 5% would likely be a catalyst for the current equity cycle to peak.



Source - RBC Wealth Management, Bloomberg, Optuma

TREND & CYCLE
2025 TECHNICAL OUTLOOK

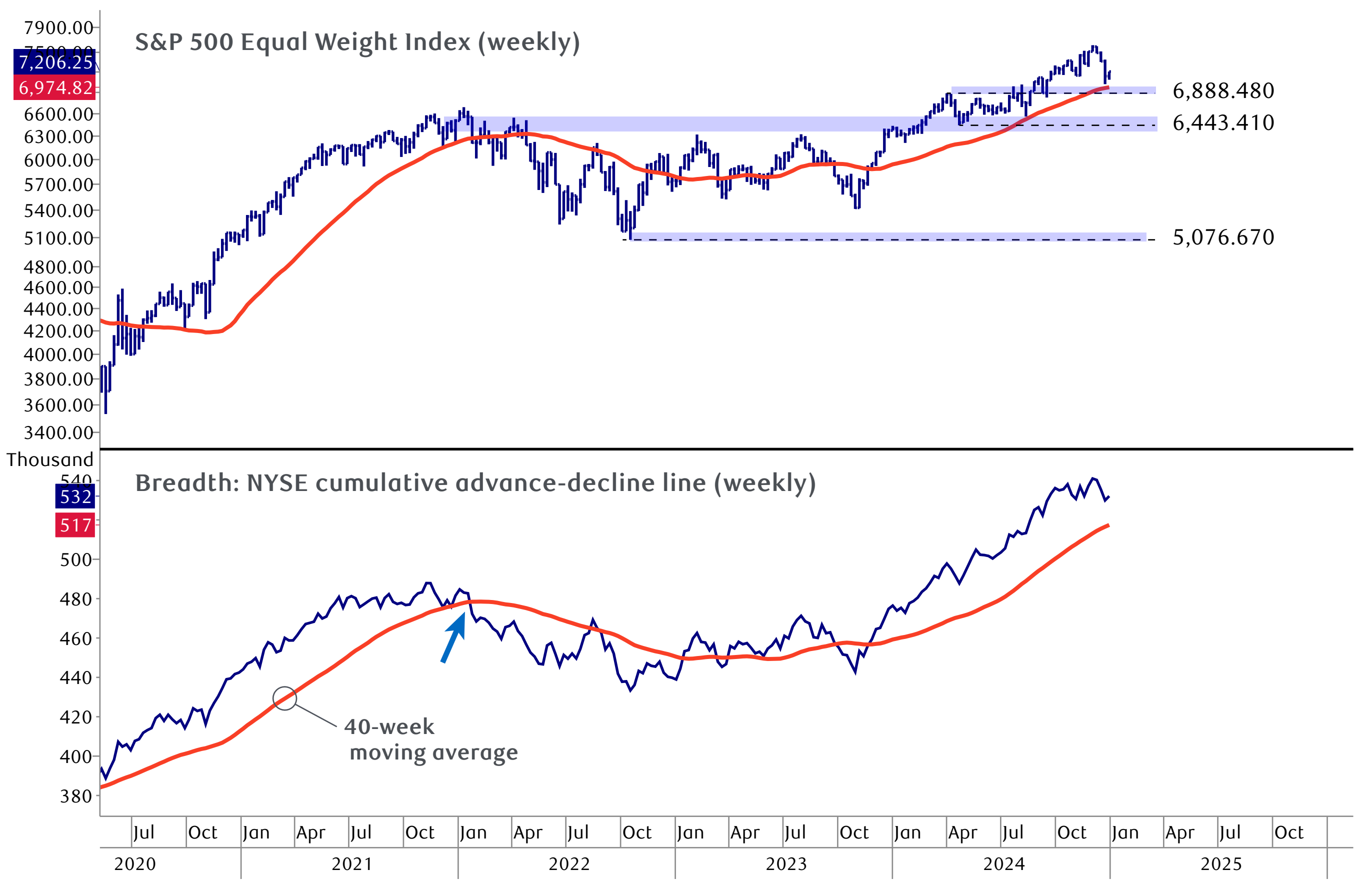
Tracking market breadth

Looking beyond the S&P 500, a major concern for investors has been the narrow leadership in a handful of large growth stocks.

The S&P 500 Equal Weight Index and NYSE cumulative advance-decline line (see charts below) remove much of the distortion caused by the surging mega-cap growth stocks and provide a gauge of how the average smaller stock is behaving.

Until late December 2024, participation (as measured by the S&P 500 Equal Weight Index and the number of stocks advancing versus declining) had been improving since Q4 2023. The key takeaway from these charts is that while a near-term pullback is underway, their trends remain positive with support beginning near their rising 40-week moving averages.

A break below the rising 40-week moving average would be of greater concern, in our view. This break was the negative technical signal that developed for the NYSE cumulative advance-decline line in Q1 2022 at the beginning of the bear market (indicated by the blue arrow). Here again, we view a move above 5% by the U.S. 10-year yield to be the main risk to the maintenance of the uptrend.



Source - RBC Wealth Management, Bloomberg, Optuma

TREND & CYCLE
2025 TECHNICAL OUTLOOK

Key levels for interest rates

With interest rates playing a dominant role in how investors value asset classes, the trend for the U.S. 10-year bond will remain a major technical focus for us through 2025.

As noted earlier, the major catalyst for equity market participation to broaden in Q4 2023 was the U.S. 10-year yield peaking at 5%, before trending lower within a range through 2024.

Our base case is that the 10-year yield will remain in that 3.25%–5.00% range through most of 2025 with one- to two-quarter swings likely to define the trading range. To track these swings, we use a simple momentum indicator (bottom panel in the chart below) which has proven useful for identifying turning points through 2024. Our expectation is that this indicator will develop another tactical peak in early Q1.

Risk: We continue to view the band between approximately 4.7% and 5.0% as an important upside threshold, and while our base case is for rates to peak under that level, we think a move above that range would signal an important breakout with the next upside level just below 6.0%, corresponding to a 161.8% extension of the 2024 trading range. As noted earlier, a move above 5% is likely to exert meaningful downside pressure on equity markets.

Source - RBC Wealth Management, Bloomberg, Optuma

TREND & CYCLE
2025 TECHNICAL OUTLOOK

Sector rotation

We think of equity sectors as falling within three main categories: structural growth, cyclical growth, and defensive.

Given the S&P 500 is dominated by large-cap growth stocks, notably in Technology and Communication Services, our technical outlook for structural growth stocks aligns with our outlook for the S&P 500 discussed above. In short, these growth stocks remain in positive trends but are, in our opinion, less timely for establishing new positions at current levels following very large two-year advances.

Cyclicals, those sectors that are the most responsive to the underlying economy, tend to be volatile, with one- to two-quarter rebounds followed by choppy, multi-month trading ranges. The S&P 500 Industrials and Financials sector chart below illustrates these multi-month swings from within a longer-term bullish uptrend that accelerated in Q4 2023 after interest rates peaked at 5%. After pausing through H1 2024, cyclicals rallied strongly through Q3 into Q4 of this past year, with the post-election rally leading both sectors to peak near technical extension levels. While both sectors remain in longer-term uptrends, the technical backdrop suggests to us that investors should remain patient for better entry points in Q1.

Lastly, defensive sectors, such as Utilities, Consumer Staples, Health Care, and Real Estate, have dramatically underperformed the S&P 500 since the bull market began in Q4 2022. While we see no evidence of a relative performance reversal developing for these areas, a growing list of what we view as defensive stocks is becoming oversold, and with the S&P 500's cycle momentum becoming advanced, we expect to see more timely opportunities developing in these sectors moving through the first half of 2025.

Source - RBC Wealth Management, Bloomberg, Optuma

GLOBAL

Equity

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Benefit of the doubt

As the new year gets underway, investors find themselves in much the same place they were 12 months ago. Back in January of 2024, following a very strong market advance through all of 2023, the S&P 500 Index looked expensive at 22x the latest 12-month earnings—$219 per index share. Adding to the perception of market vulnerability at the time was the fact that most of the earnings growth that year, as well as virtually all the price-to-earnings (P/E) valuation premium which had built up, was largely attributable to a concentrated group of megacap growth stocks—the so-called "Magnificent 7" (Alphabet, Amazon, Apple, Meta, Microsoft, NVIDIA, and Tesla).

The S&P 500 minus those very strong performing stocks was trading at an easier-to-justify P/E multiple in the mid-to-high teens. The same was true for all the major equity indexes outside the U.S., including Canada's TSX Composite and the MSCI indexes for the UK, Europe, and Japan. These non-U.S. indexes had no exposure to the "Magnificent 7" and comparatively few megacap growth stocks of any stripe.

Fast forward to today and one finds the picture looks much the same but different. A second consecutive year of powerful advances for the S&P 500 and the TSX is behind us. Gains for Europe, the UK, and Japan in the low double-digits were above-average but less dynamic. Valuations moved higher as well. The S&P 500 ended the year at a rich 24.4x full-year consensus earnings estimates of $243 per share, up from 22x a year ago. Most other markets also added a couple of multiples to their valuations, suggesting to us that investors everywhere have become more confident and comfortable over the course of the past 12 months.

That interpretation appears to be borne out by several sentiment indicators:

Equity views

Region	Previous	Current
Global	=	=
United States	=	=
Canada	=	=
Continental Europe	=	–
United Kingdom	–	–
Asia (ex Japan)	=	=
Japan	=	=

\+ Overweight; = Market Weight; – Underweight
Source - RBC Wealth Management

- The percentage of respondents to the University of Michigan's Survey of Consumers who have expected stock prices to rise has been rising sharply since the 2022 lows, albeit without yet reaching new highs.
- A similar question in the Conference Board's Consumer Confidence Survey for October saw 51.4% of respondents expecting higher stock prices 12 months hence, the highest positive response since the question was first posed in 1987. The November response surged past the October high-water mark to post a new all-time high of 57.2% before easing back to a still-elevated 52.9% in the December survey.
- The bullish positioning in S&P 500 futures by funds and reporting institutions is off only fractionally from the all-time high set in October, which itself was well beyond previous peaks.

Elevated readings from such indicators do not mean the S&P 500 can't move higher. But they do form part of a larger picture in which there looks to us to be a potentially precarious balance between expectations for a richly valued market to go even higher on the part of an historically high percentage of individual investors at a time when fund managers have committed very one-sidedly to a bullish outcome.

GLOBAL EQUITY

Meanwhile, over the past several months the 10-year U.S. Treasury bond yield has moved up from 3.63% to 4.58%. This has made those anticipated stock market gains harder to achieve because higher interest rates make the discounted present value of all future earnings (and hence the value of an individual company or the market) worth less than it had been.

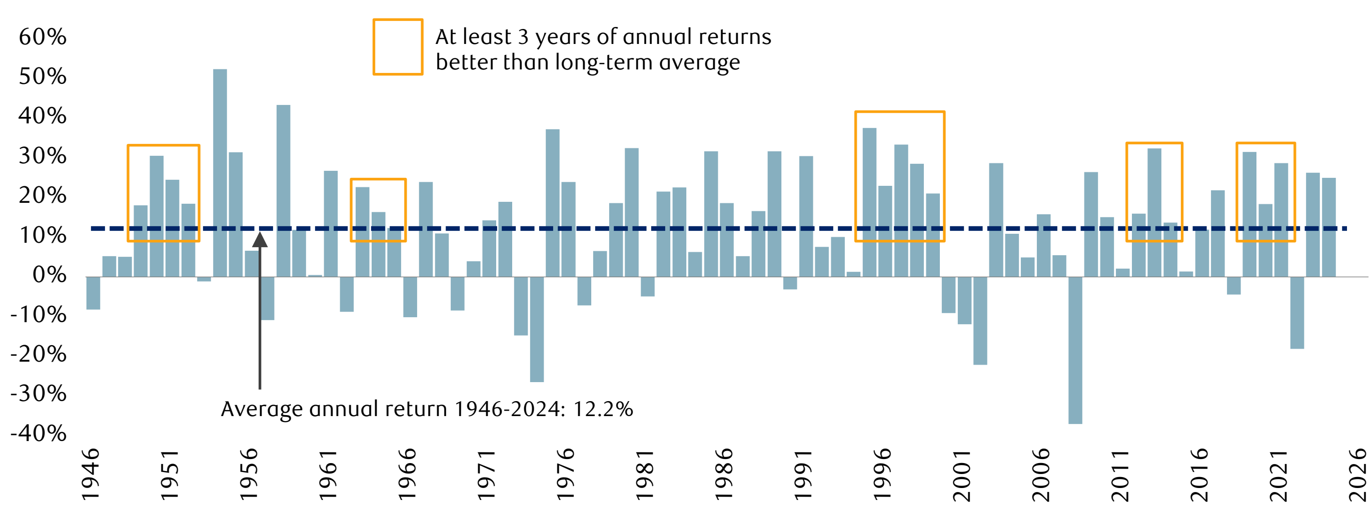
In order to overcome this value compression induced by higher bond yields, we will need to see those yields coming down or future earnings growing faster than investors expect, or some combination of the two if the market is to rise sustainably from here. But getting bond rates down and earnings up will be a challenge. S&P 500 consensus earnings growth is already forecast to accelerate to 13% this year from 11% in 2024. For earnings growth to remain in double digits beyond 2025 would probably require faster GDP growth than the market is forecasting, a situation that would likely be inflationary. There is not a lot of excess capacity in the U.S. economy, particularly in the labor market where the threat of deportations looms.

For now, however, investors may see strong earnings growth into 2025 and beyond as being plausible, potentially opening a path to more new highs for the stock market and perhaps even a higher P/E multiple. (Historically, two above-average years back to back in the market has not ruled out a third or a fourth—see chart.) But GDP growth looks to have slowed in 2024 and most forecasts (including our own) have it slowing further in 2025. If quarterly data starts to make that downshift in growth apparent to investors by the middle of the year, then we believe today's complacency about the direction of stock prices is likely to erode.

For our part, we think portfolios should stay committed to equities up to but not beyond their long-term targeted exposure. Our Technical Outlook for the year ahead argues that upward momentum for the S&P 500 may be peaking, which would suggest a more challenging period for share prices might arrive in the second half.

We continue to monitor market breadth closely. So far, so good. As long as the direction of the majority of S&P 500 stocks continues to move in sync with the index itself, our preference will be to give this uptrend the benefit of the doubt. But with the technical work indicating that an inflection point may arrive later in the year, for now "cautious, watchful, but invested" will remain our watchwords.

S&P 500 annual returns



Source - RBC Wealth Management, Standard & Poor's

GLOBAL

Fixed income

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The Fed at risk of a missed approach?

The U.S. Federal Reserve's policy meeting in December marked a sharp reversal in sentiment compared to the September meeting. In the autumn, as the chart shows, just three policymakers saw further upside risks to inflation, with the majority seeing the risks as balanced and inflation on a glide path back to the Fed's 2% target. That flipped almost entirely in December with the vast majority seeing renewed upside risks.

The key contributors to the Fed's change in thinking, in our view, were a lack of further progress in some recent inflation data, paired with heightened inflationary risks and uncertainty around the potential policy plans of the incoming Trump administration.

The net result is that Fed policymakers halved the number of projected interest rate cuts in 2025, from four to just two, suggesting rates could settle at a 3.75% to 4.00% range sometime this year, down from 4.25% to 4.50% currently. After consecutive rate cuts at the September, November, and December meetings, we expect the Fed to skip a rate cut at its meeting this month, followed by a cut in March. We believe the path from there will depend on how the economic data develops.

While developments at the Fed jolted U.S. fixed income markets in mid-December, with the benchmark 10-year Treasury yield touching its highest levels since April 2024 at over 4.6%, global central banks remain on track for further policy easing in 2025, in our view. The Bank of Canada, amid soft economic growth, looks set to do

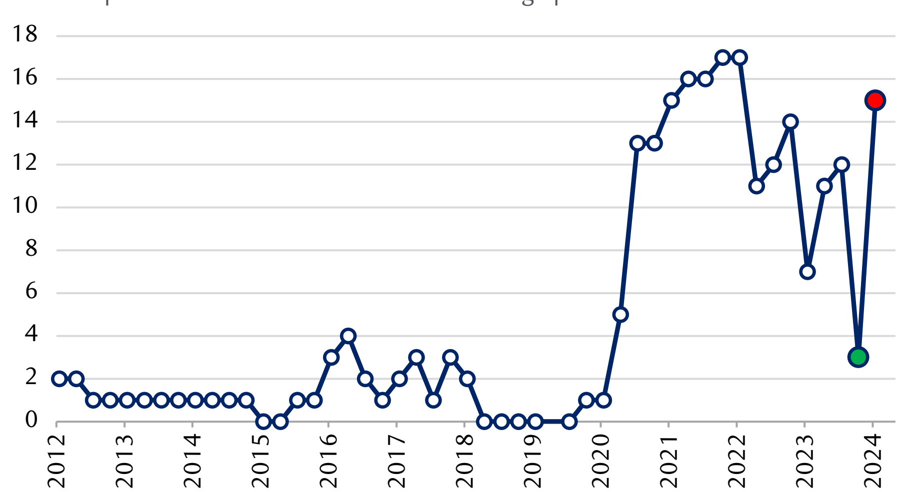
Fixed income views

Region	Gov't bonds	Corp. credit	Duration
United States	–	=	3–7
Canada	+	=	3–7
Continental Europe	+	=	3–7
United Kingdom	+	=	3–7

+ Overweight; = Market Weight; – Underweight
Source - RBC Wealth Management

Renewed inflation risks?

Federal Open Market Committee members seeing upside risks to inflation

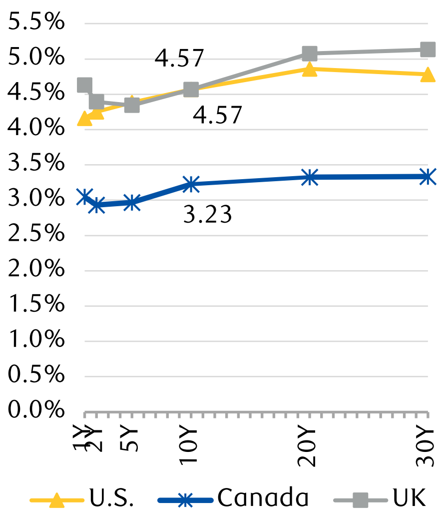


Note: Includes the 12 voting members of the FOMC and seven alternates.
Source - RBC Wealth Management, Bloomberg, Federal Reserve

GLOBAL FIXED INCOME

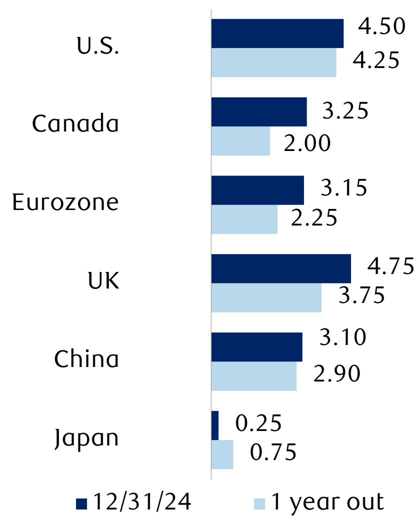
the most by cutting rates to 2.00% by year-end per RBC Capital Markets, compared to 3.25% currently after a 50 basis point (bps) cut in December. We see the Bank of England cutting by 100 bps to 3.75% and the European Central Bank lowering rates by 75 bps to 2.25%.

Sovereign yield curves



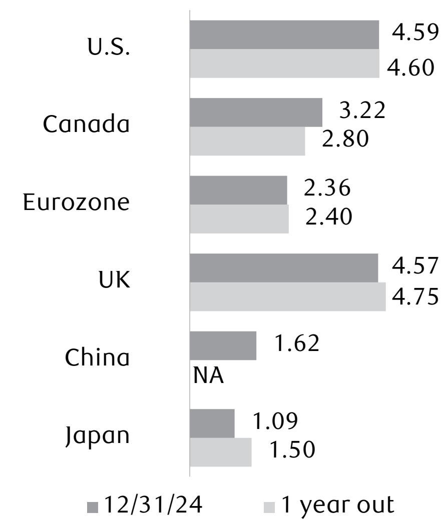
Source - Bloomberg; data through 12/31/24

Central bank rates (%)



Source - RBC Investment Strategy Committee, RBC Capital Markets forecasts, Global Portfolio Advisory Committee, RBC Global Asset Management

10-year rates (%)



Note: Eurozone utilizes German Bunds.
Source - RBC Investment Strategy Committee, Global Portfolio Advisory Committee, RBC Global Asset Management

U.S. RECESSION
Scorecard

New year, same Scorecard

For most of the first half of last year the Scorecard—that had been all expansionary "green" in 2021—looked to be sliding inexorably toward all recessionary "red." However, the second half saw little to no movement among the indicator ratings. And, as the U.S. economy enters 2025, the Scorecard's leading indicators are looking more undecided than ever. One or two could ease back into more optimistic ratings if some modestly positive trends were to firm up, while others could become more negative.

Many are of the view that time has run out on the possibility of a recession arriving in the wake of a Fed rate-hiking cycle that looks to be over. It would be nice to think so, but we think there are at least two "clocks" still ticking.

Recessions since the early 1950s have started an average of 10 quarters after the first Fed rate hike. We have just completed the 11th. For more than half those recessions, the first-hike-to-recession gap was longer than the 10-quarter average.

And, as noted below, the yield curve had de-inverted before or just as the recession got underway for seven of the past 10 U.S. recessions. De-inversion in the current instance occurred in November.

On balance, we are of the view that a mixed Scorecard argues for a watchful, cautious approach for investors.

Yield curve

In November, the yield curve finally returned to a normal positioning—that is, short-term Treasury yields are once again lower than long-term yields. Most of this shift from inversion to normalization of the curve occurred in the last four months of the year as a succession of Fed rate cuts lowered short yields by about 100 basis points. Over the same interval, the 10-year Treasury yield was heading in the opposite direction, rising by about 100 basis points, as investors worried that inflation might stay higher than hoped under the influence of a stronger-than-expected U.S. economy and the prospect for broad implementation of tariffs.

This crossover late last year ended the longest-ever inversion of the curve—29 months—from July 2022 to November 2024. The good news is that the drag from the extended period of tight monetary conditions

U.S. Recession Scorecard

	Status		
Indicator	Expansionary	Neutral/ Cautionary	Recessionary
Yield curve (10-year to 1-year Treasuries)			✓
Unemployment claims		✓	
Unemployment rate			✓
Conference Board Leading Economic Index			✓
Non-financial corporate cash flows	✓		
ISM New Orders minus Inventories		✓	
Fed funds rate vs. nominal GDP growth			✓

Source - RBC Wealth Management

U.S. RECESSION SCORECARD

should gradually abate across the economy. However, the historical record would argue there remains room for a recession. In seven of the past 10 U.S. recessions, the yield curve had de-inverted before or just as the recession got underway.

Occasionally, Fed tightening produced a soft landing rather than a recession. In those instances, while interest rates rose by a meaningful amount, banks did not overtly tighten lending standards. However, whenever they did, the combination of high rates and tight lending conditions produced a recession.

In this latest Fed tightening cycle, a growing majority of banks progressively raised lending standards alongside Fed rate hikes. And even with the Fed having cut its funds rate by 100 basis points, for most categories of loans a majority of banks (albeit a narrowing one) continue to raise lending standards.

Nor have loan rates come down appreciably:

- Credit card rates today average close to 24% vs. 16% three years ago;
- Car loans cost just shy of 9% vs. 4.5%; and
- 30-year mortgage rates sit at 7.2% vs. 3%.

This "stickiness" of both loan rates and bank lending standards after four months and 100 basis points of Fed rate cutting conforms with the notion that monetary policy changes act with a lag of six months to a year. To move the yield curve rating out of the "red" column we would want to see the gap between short and long rates widen further accompanied by a measurable decline in borrowing rates with a clear majority of banks easing lending standards.

Conference Board Leading Economic Index

The U.S. leading index rose by 0.3% in November after 30 straight months of decline. That increase is being interpreted by the Conference Board as signaling no U.S. recession is imminent. For our part, we would need to see several months of a sustained reversal in trend before moving this indicator to a more benign rating.

Unemployment claims

Claims set a low for this cycle in September 2022, but subsequently they have failed to establish the sustained upward trend that typically precedes the start of a recession. The weekly count jumped sharply higher in early December, but the seasonal adjustment factor around the holiday period is generally regarded as unreliable. We think "undecided" is the correct interpretation of the claims data as things stand.

Unemployment rate

The unemployment rate usually surges higher just before or just as a recession is getting underway. Typically, it takes an upward move of as little as half-of-one percentage point from the cycle low to signal the start of recession. The low for the unemployment rate was set at 3.4% in April 2023, so that condition has been met. However, as with claims, the anticipated "surge" higher has been more of a "creep" to a recent high of 4.3%. The unemployment rate sits at 4.2% as of this writing.

Also, like claims, seasonality adjustments in December and January may be suspect. That concern notwithstanding, were the unemployment rate to settle back below 4%, we would re-rate this indicator to "neutral/cautionary."

U.S. RECESSION SCORECARD

ISM New Orders minus Inventories

The difference between the New Orders and Inventories sub-indexes of the ISM Purchasing Managers' Index has turned negative near the start of most U.S. recessions. But it has also registered occasional false positives—signaling a recession was imminent when none subsequently arrived. Moreover, this indicator only relates to activity in the manufacturing sector (some 15% of the U.S. economy) and is derived from a survey rather than hard data. For those reasons, we look at it as a corroborative indicator rather than a decisive one taken on its own.

After setting its most recent low in September 2022, this series rose steadily (we use a three-month moving average) and moved back above zero in August 2023. It has managed to stay above zero over the intervening 16 months, despite the fact the new orders component by itself remained predominantly negative, recording only three positive monthly readings over the past 27 months. The rating for this indicator remains at "neutral/ cautionary."

Fed funds rate vs. nominal GDP growth

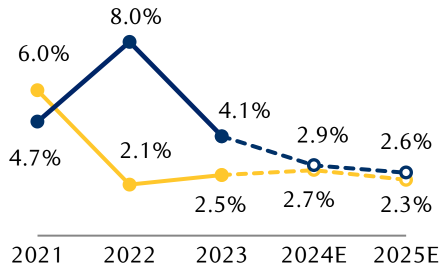
The fed funds rate has risen above the six-month annualized run rate of nominal GDP either before or at the start of every recession in the past 70 years. (Nominal GDP is GDP not adjusted for inflation.) That GDP run rate has been declining since its pandemic reopening high of 23% recorded in Q4 2020. By the end of last year, it had slowed to 6.7%, still above the 5.50% fed funds rate. However, for Q2 and most of Q3 the six-month annualized run rate of nominal GDP was running below where the fed funds rate sat at the time, meeting the condition observed before every recession. This indicator remains in the recessionary "red" column.

Non-financial corporate cash flows

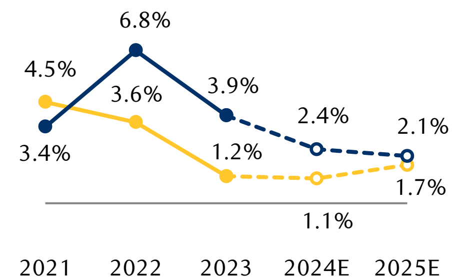
This gives an indication of the ability of such businesses, in aggregate, to internally fund any capital spending they want or need to do. Historically, whenever it has posted a year-over-year negative reading, a decline in corporate capital spending has typically followed, either indicating a recession is coming or a deepening one is already underway. These cash flows, while down from their pandemic peak, are still above a negative crossing point as of Q3, which leaves it as the sole indicator still giving the U.S. economy an expansionary "green" light. There is a long lag time before this data is reported with the Q4 release not coming until March.

KEY
Forecasts

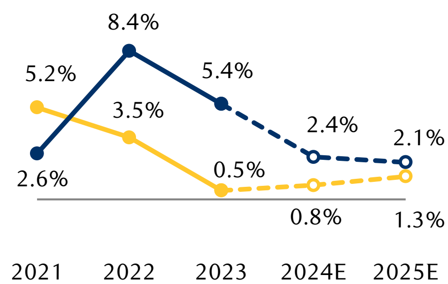
United States



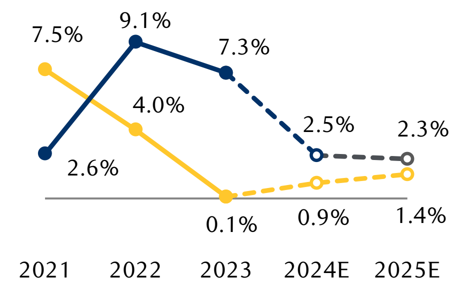
Canada



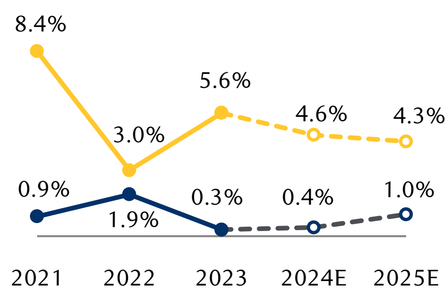
Eurozone



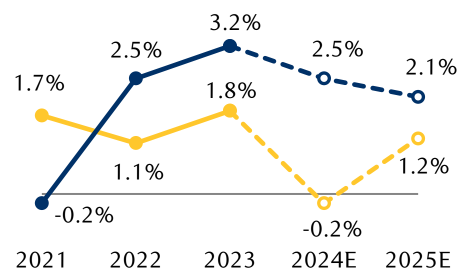
United Kingdom



China



Japan



Real GDP growth

Inflation rate

Source - RBC Investment Strategy Committee, RBC Capital Markets, Global Portfolio Advisory Committee, RBC Global Asset Management, Bloomberg consensus estimates

Research resources

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As of December 31, 2024

			Investment Banking Services Provided During Past 12 Months	
Rating	Count	Percent	Count	Percent
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