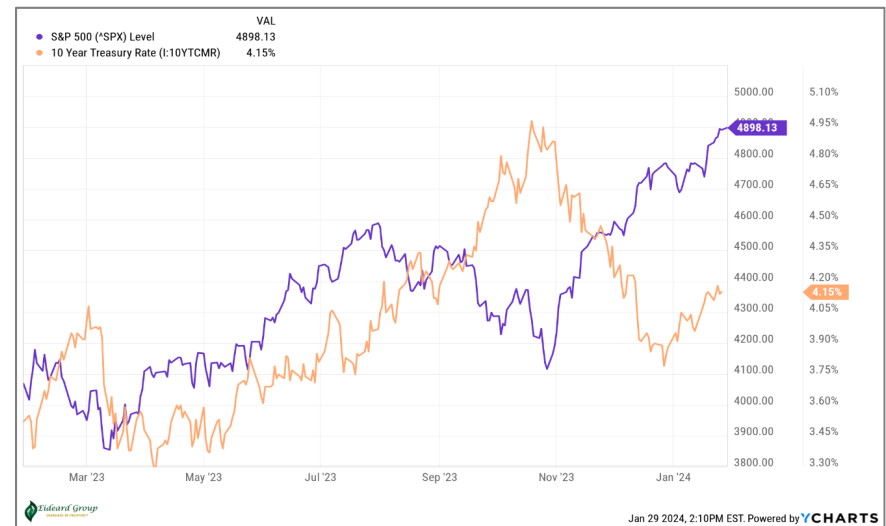


2023 Year in Review

Pushing back on overly-hyped recessionary expectations, and even a soft landing, the economy displayed extraordinary resilience in 2023! But for a couple of hiccups early on and later in the year, its resilience framed the conditions for a solid year for financial market returns. Surely the outcome was much welcomed after having suffered the pain of the 2022 bear market for both stocks and bonds alike (something uniquely rare in history). We'll all remember 2022's emotional ride, ignited by the FED's shift from easy money to unprecedented and precipitous rate hikes, which rippled through the economy and the markets sparing little in their path. Thankfully, most of the damage done to destroy inflation concluded just as 2022 gave way to the New Year, coupled with a nascent optimism that the bear market might succumb to a new bull market cycle.

From last January through the about mid-year, the stock market rallied to recover much of what had previously been lost. While it's true that the unabated gains in the first 5 months were almost exclusively attributable to a recovering technology sector, and more specifically the so-called "magnificent seven tech companies", by June and July that narrow participation blossomed across all stock sectors. To us, this unchallenged trend was a potent sign that the bear market was finally relinquishing to a new bull market cycle. Meanwhile, on the flip side, bonds which had also previously suffered significant unrealized losses through 2022 began a similar healing process, as prices firmed up rapidly to narrow their losses. At that juncture, we were confident that the old axiom "trade in May and go away" was again applicable as we embarked on the lazy days of summer! It was not until late August into early September that cumulus clouds began re-appearing in an otherwise bright sky. And with that, the month of September (as it is so often known to do)

ushered in another episode of sharp market volatility and investor angst. Almost overnight, the volatility index (VIX) spiked from its summer flat line. Presumably, this often recurring phenomena is lodged, at least in part, in behavioral psychology; the notion that with the passage of Labor Day, it's once again time to roll up the sleeves, return to work and perform a reality check on all matter of things, including how our portfolios may have performed over the quiet summer months. In this case most investors knew it was a summer of fruitful performance and so, on first blush, perhaps profit taking had ignited the volatility. But this time around the volatility was too sudden, markedly fierce and relatively lengthy to suggest the cause was simply related to reaping profits. Something more menacing was at work, after all September and October's downside risk was the worst we had experienced all year. Keen on understanding why, our homework quickly linked cause with effect. The conclusion was as simple as the daily change in the 10-year Treasury bond, arguably the most monitored financial benchmark in the US, if not the world.



As the accompanying chart clearly illustrates, there was almost near perfect negative correlation between the daily rising T-yield, which had spiked up and through 5%, its highest level in at least a decade or more, and the price consolidation which occurred from September through October 27th when the stock market finally bottomed. Then, almost as quickly as it had surged, the yield reversed course to reignite the price rallies we had witnessed in November and December. Thankfully at the end of the day, the stock market had not only recovered but edged up to new peaks, while the bond market delivered solid total returns.

Another matter of curiosity that emerged for us in 2023 occurred when the Bureau of Economic Analysis (BEA) announced its first estimate of 3Q23 GDP growth: a whopping +4.9%. This was more than double the previous quarter's estimate and oddly reminiscent of the post-Covid consumer surge. This productivity level was counterintuitive, especially given the interest rate environment. We suspected there'd either be a major revision downward (which often occurs in 2nd and 3rd estimates) or there was something more positive at work. Either way it was a quandary which no market pundit seemed to adequately address, at least not until we discovered a *Wall Street Journal* article published on 1/15/24. To summarize their thesis: *From 2020-2022, when businesses could not meet post-Covid's unleashed demand, the lack of virtually everything supply side driven (from parts and labor to transport capacity along with government stimulus) drove prices through the roof. But businesses typically don't sit idle when there is an opportunity to profit from high prices and unmet demand. They boost output by all means possible – raising capital, reorganizing production and boosting capacity, all in an effort to "Make hay while the sun shines!"* And so while there is always a lag effect from such dynamics, the effect peaked and the "hay" was harvested in the third quarter's GDP

number! Satisfied by a logical narrative, we can now close the books on 2023 and the solid market performance it delivered!

Broad Market Indexes	QTD	YTD
Dow	13.09%	16.18%
S&P 500 Index	11.69%	26.29%
Nasdaq	13.79%	44.64%
Russell 2000 Index	14.03%	16.93%
MSCI World Index	11.42%	23.79%
MSCI World Small Cap ex-USA Index	10.60%	12.62%
Bloomberg 10 Year Municipal Bond Index	7.47%	5.78%
Bloomberg Aggregated Bond Index	6.82%	5.53%
Bloomberg High Yield Index	7.16%	13.44%

Looking Forward

As we look to the New Year and January's close, favorable economic and financial market trends continue. At the core of investor optimism is the likelihood that the FED, having neared its terminal rate and by most measures succeeded in driving inflation meaningfully closer to its 2% target, will likely pivot and begin cutting rates before year end. Powell is seen delivering a softer message these days but the question still remains: *How many cuts and when?!* This is where most would agree the disconnect lies (the market's perception vs how much and when the FED delivers). On this score only time will tell!

In the meantime, however, most statistics still portend overall economic resilience. The initial estimate of 4Q23's growth came in at +3.3%, a bit slower but still very respectable. As we mentioned earlier, headline inflation is down to +3.5%. Employment remains

firm at 3.7%. Consumer sentiment is up +21% year over year and consumer spending remains robust, despite that credit card debt has reportedly topped \$1 Trillion for the first time. Moreover, it's an election year which historically proves to be neutral if not positive for the markets. Against all these positives, however, there is a growing concern for increasing geopolitical risk in the Middle East. As we know, the US has once again deployed significant force structure in and around the region; one that is definitely playing around the edges with Iran, the Houthis and other regional proxies surrounding Israel. Our hope is that the US show of force coupled with defensive and prudent tactical strikes, as may be necessary, will be sufficient to ward off a larger engagement.

In the meanwhile, however 2024 unfolds, you can be sure we will be monitoring from all angles and offer you our best professional advice. Best wishes "to all of us" for another prosperous and healthy New Year!

Eideard Group

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