W A I N W R I G H T   I N V E S T M E N T   C O U N S E L , L L C

FINANCIAL MARKETS HIGHLIGHTS

Fourth Quarter 2023

The fourth quarter began with the capital markets generally weak, following a down third quarter, but markets rallied hard in November and December and regained all of the ground lost and then some. Ultimately, the S&P 500 index of large and mega-cap stocks had its best quarter since 2020, and the tech-heavy NASDAQ 100 index had its best year since 1999. With such a grand reversal, one can reasonably wonder: How did we get here?

Recall that the Federal Reserve ("Fed") has been "tightening" monetary policy, observed most visibly via raising short-term interest rates, since Q1 2022. Its objective was to quell the runaway inflation induced by unprecedented monetary stimulus and snarled supply chains that resulted from the global pandemic. The effect of higher interest rates being to induce savings and impede credit-reliant investment, thus slowing the economy and, therefore, placing downward pressure on corporate earnings. The opposite is also true though; lower interest rates stimulate the economy, corporate earnings and, therefore, stock prices.

In response to inflation data moving aggressively to more normal levels (Nov-23 all-item consumer prices were +3.1% for the trailing 12 months vs. a peak of +9.1% in Jun-22), the Fed began signaling that more rate hikes were unlikely and, indeed, lower interest rates in 2024, 2025 and 2026 were the consensus expectation amongst its Federal Open Market Committee participants. With that, markets soared, both stock and bond, and investors experienced one of the better two-month stretches in recent memory.

The S&P 500 gained 11.7% during the quarter and 26.3% for the year. Nine of its ten sectors were positive during the period, and five of the ten finished with quarterly gains greater than 10%. The top performing sectors were Technology (17.2%), Financials (14.0%) and Industrials (13.1%). Only Energy was down for the quarter (-6.9%).

For much of the year there was more than a little consternation, including from yours truly, that the Magnificent Seven of mega-cap stocks were the disproportional driver of market returns. The lack of market "breadth" was concerning, particularly so if one believes in the merit of diversification. Market action during Q4 alleviates some of that concern as small-company, value-oriented, and international stocks all meaningfully participated in the rally. All of this taking place in spite of the horrific disasters transpiring in the Middle East and the Ukraine.

The typically staid bond market chose to join the party. The Bloomberg Aggregate Bond Market index returned -2.8% for the year through October, but roared during November and December to end the quarter and year up

Selected Index Returns (%) as of December 31, 2023 (Source: Morningstar Direct). 3, 5, 10 year returns are annualized.

	Oct.	Nov.	Dec.	QTR	YTD	1 Year	3 Year	5 Year	10 Year
S&P 500	-2.10	9.13	4.54	11.69	26.29	26.29	10.01	15.69	12.03
S&P 400	-5.34	8.51	8.72	11.67	16.44	16.44	8.09	12.62	9.27
Russell 2000	-6.82	9.05	12.22	14.03	16.93	16.93	2.22	9.97	7.16
Wilshire U.S. REIT Index	-4.55	10.56	10.19	16.30	16.10	16.10	7.52	7.56	7.72
MSCI EAFE	-4.05	9.28	5.31	10.42	18.24	18.24	4.02	8.17	4.28
MSCI Emerging Markets	-3.89	8.00	3.91	7.86	9.83	9.83	-5.08	3.69	2.66
Bloomberg U.S. Aggregate Bond	-1.58	4.53	3.83	6.82	5.53	5.53	-3.32	1.10	1.81
Bloomberg High Yield	-1.16	4.53	3.73	7.16	13.44	13.44	1.98	5.37	4.60

6.8% and 5.5%, respectively. With investors expecting rate cuts in the future, bond yields fell, and bond prices rose accordingly. Long-term U.S. Treasuries were the best performing bonds during the quarter. The iShares 20+ Year Treasury Bond ETF gained 12.9%. Corporate high yield bonds were also strong, in part due to the notion of a "soft landing" gaining traction (*i.e.,* the economy avoiding recession despite the Fed's aggressive interest rate hiking cycle). The Bloomberg High Yield index returned +7.2% for the quarter and +13.4% for the year.

Commodities and commodity-related sectors were mixed during the quarter. Gold and silver returned 11.5% and 7.1%, while natural gas and oil were down 4.8% and 16.0%, respectively. The dollar declined about 3% against a broad basket of foreign currencies compiled by the St. Louis Federal Reserve. Bitcoin, for those masochists to whom the gyrations of penny stocks are far too tame, rallied 61.1% during the quarter.

The Fed's signaling of interest rate cuts induced the Q4 rally, but the importance of an incredibly resilient U.S. economy in the face of a historically aggressive rate hiking cycle cannot be understated, particularly when looking at the year as a whole. Real GDP increased at an annual rate of 4.9% during Q3, and unemployment at 3.7% remains lower than historical averages. The annual inflation rate slowed to 3.1% in November, down from 3.2% in October and 3.7% in both August and September.

Following last quarter's trend, the outlook for corporate earnings remains positive. Yardeni Research and S&P project 2024 earnings growth in excess of 10%. We are reminded of the notion that, in the short-term, the stock market is a voting machine, but in the long-term it is a weighing machine. Presently votes are being cast largely based on interest rate expectations. Over time though, stock prices reflect a company's ability to grow its earnings, assets and dividends. On that score, Corporate America remains undefeated.

From all of us here at Wainwright, we hope you had a happy holiday season, and we look forward to continuing to serve you in 2024. Happy New Year!

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