TILLER
PRIVATE WEALTH

Q4 2023 Market Update

Market Snapshot

Dow Index 37,690	**10-year Treasury rate** 3.88%
S&P 500 Index 4,770	**1-year Treasury rate** 4.79%
NASDAQ Index 15,011	**Prime mortgage rate** 8.50%

**As of 12/29/2023*

By the Numbers

- The S&P 500 closed at 4770 on 12/31/2023, just 4 points higher than 12/31/2021. This docile change masks a drop of nearly 28% at the low of October 13, 2022. While 'flat' over 2 years, the index is up ~45% over the past 3 years, reminding us that the markets never move in a straight line
- GDP grew 2.4% in 2023, defying the January 2023 predicted annual decline of 0.3%
- The Consumer Price Index grew 3.1% this past November on a year-over-year basis, in marked contrast to 9.1% in June 2022
- Unemployment is still only 3.7%
- Interest cost on US debt is expected to overtake defense spending within the next 4 years

Soft Landing?

2023 marked an inflection point for markets with strong gains across both stocks and bonds. The S&P 500, Dow, and Nasdaq (Driven by the Magnificent 7) generated exceptional returns of 26.3%, 16.2%, and 44.7% with reinvested dividends last year, respectively. The S&P has come full circle and is now only a fraction of a percentage point below the all-time high from exactly two years ago. The U.S. 10-Year Treasury yield climbed as high as 5% in October before falling to end the year around 3.9%, pushing bond prices higher in the process. International stocks also performed well with developed markets returning 18.9% and emerging markets 10.3%.

Last year's positive returns occurred despite historic challenges including, rapid Fed rate hikes, debt ceilings and budget battles in Washington, the worst banking crisis since 2008, the ongoing war in Ukraine, the conflict in the Middle East, and cracks in China's economy. If you had shared these headlines with an investor at the start of 2023, they would probably have assumed there would be a worsening bear market or a deep recession.

The key factor driving markets the past few years has been inflation, forcing the Fed to raise interest rates, slowing growth, hurting corporate profits, dampening consumer spending, and acting as a drag on bond returns. This is exactly what occurred in 2022 but many of these effects reversed in 2023 as inflation rates improved.

Thus, the recession that was highly anticipated by markets a year ago has not yet occurred. Remember, a recession is defined as a negative decline in GDP for two consecutive quarters; GDP grew by 2.4% in 2023. While many still expect economic growth to slow this year, it's not unreasonable to suggest that the Fed could achieve a "soft landing" in which inflation stabilizes without causing a recession. This is why both markets and Fed forecasts show that they could begin to cut policy rates by the middle of the year.

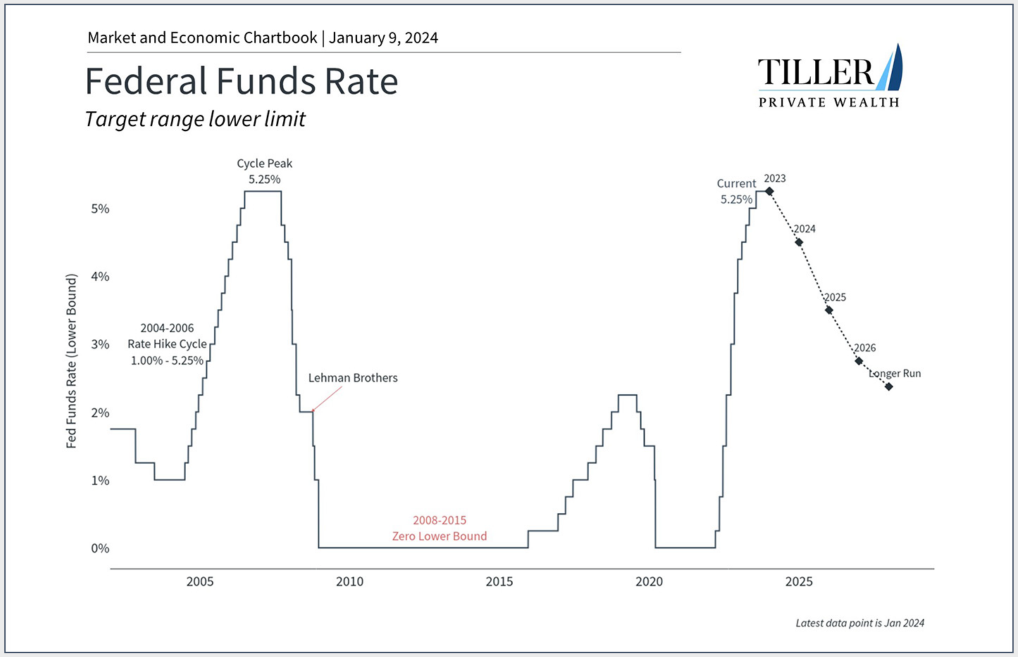
There are also signs that earnings growth is recovering. Earnings-per-share for the S&P 500 are expected to have been flat in 2023, but Wall Street consensus estimates suggest that they could grow by double digits each of the next two years. While this will depend on the path of economic growth, any increase in earnings will help to improve valuations and support the stock market.

Improving inflation coupled with a historically strong job market have helped the Fed to achieve its policy objectives. It is certainly too early to declare victory, but many, including us, expect the Fed to begin cutting rates in 2024. While hard to predict exactly what the Fed may do this year, the fact that rates could begin to fall could help to support financial markets and the economy.

While the past twelve months have been positive for investment portfolios, investors should not become complacent. Volatility in the stock market is both normal and expected with even the best years experiencing short-term swings. Rather than trying to predict exactly when these pullbacks will occur, it's more important for investors to hold diversified portfolios that can withstand unforeseen events.

Chart of the Month

The Fed is expected to cut rates in 2024



Sources: Clearnomics, Federal Reserve

Data sources: YCharts, US Treasury Dept, Clearnomics, Bankrate.