CLARO ADVISORS

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Market Insights
A Strong Finish to an Up and Down 2023

It was anything but a smooth ride for financial markets in 2023. The year started off with a robust rally in January, followed by two significant sell-offs in the Spring and Fall, and finished with a historically strong "Santa Claus" rally to end it. Going in there were meager expectations as inflation concerns and recession fears dominated sentiment. And there was plenty of drama and headwinds throughout as investors were faced with a bout of geopolitical uncertainty (Ukraine/Russia war), a regional bank crisis (Silicon Valley Bank failure), and spiking interest rates. Despite the headwinds, financial markets finished the year with broad strength across asset classes as continued consumer spending, low unemployment, an end to Federal Reserve tightening and the exuberance around artificial intelligence (AI) becoming a new growth catalyst helped provide investors a boost of optimism and a reminder to why it's important to remain disciplined throughout even among an abundance of uncertainty.

- **Large Company** stocks rose +11.2% in the 4th Quarter to finish +24.2% higher for the year[1,2]
- **Small Company** stocks rose +13.6% in the 4th Quarter to finish +15.1% higher for the year
- **International Developed** companies advanced +10.1% in Q4 to finish positive +15% in 2023
- **Emerging Market** equities grew +7.4% over the last three months to finish the year +7%
- **Fixed Income** securities also recovered +6.8% in Q4 and ended +5.5% for the year

The hope is that markets continue advancing into 2024 and that valuations aren't getting too far ahead. As we have come to know, markets are forward-looking and based on current levels the expectations are for a continued rebound in the coming year. Still, there likely will be some bumps along the way. As the Federal Reserve maintains its restrictive monetary policy, there are plenty of risks that could slow down the market's advancement and lead to increased volatility. Some of the more headline worries include a

[1] Data Sources: https://ycharts.com/indices
[2] "Large companies" as indicated by the S&P 500 index; see Financial Market Data table for the indexes references above

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slowing economy, sticky inflation, "higher for longer" interest rates, and even political risk as we head into an election year.

As is often the case when markets climb the proverbial "wall of worry", these risks to the economy become more muted over time. As they do, markets should better reflect the imbedded high expectations for growth and continue looking forward to an even brighter future.

2023 vs the history books

2023 was quite notable from a historical perspective. The S&P 500 closed the year on a winning streak gaining for nine consecutive weeks and rising 13.7%, its longest such streak since January 2004. In the past 50 years there has only been one longer streak which occurred in 1985. The percent gain over the period is also significant. Of the three other streaks that lasted as long or greater, only the twelve-week rally of 1985 surpasses it with an 18% return.

2023 also ranks as the 13th best year for the S&P 500 since 1960. Of the other twelve, the following year the index gained on average 8% indicating that markets could continue to be supportive. While we don't expect 2024 to surpass 2023 in performance, there are catalysts that could propel markets further including a less restrictive Federal Reserve and an increasing corporate earnings outlook. While the "magnificent seven" stocks of Amazon, Apple, Google, Meta, Microsoft, Nvidia, and Tesla took the spotlight in 2023 accounting for 2/3rd of the S&P 500 gain. The remaining 493 stocks that make up the S&P 500 could prove to be the "supporting cast" that propels markets in 2024.

Financial Market Data				
	December	**December**	**Q4**	**2023**
U.S Stock Markets	**Closing Price**	**Monthly**	**Quarter**	**YTD**
S&P 500 Index Price	$ 4,769.83	4.4%	11.2%	24.2%
Dow Jones Industrials	$ 37,689.54	4.8%	12.5%	13.7%
NASDAQ Composite	$ 15,011.35	5.5%	13.6%	43.4%
Russell 2000 Index	$ 2,027.07	12.1%	13.6%	15.1%
International Stock Markets	**Closing Price**			
MSCI EAFE Index	$ 2,236.16	5.2%	10.1%	15.0%
MSCI Emerging Markets Index	$ 1,023.74	3.7%	7.4%	7.0%
U.S. Fixed Income	**Closing Price**			
90 Day T-Bill	$ 217.10	0.5%	1.4%	5.1%
Bloomberg U.S. Aggregate	$ 2,162.00	3.8%	6.82%	5.5%
Bloomberg Municipal	$ 1,321.87	2.3%	7.89%	6.4%
	Closing Price			
Gold	$ 2,078.40	2.1%	11.1%	14.6%
Oil (WTI Spot)	$ 71.65	-5.3%	-21.1%	-10.6%
Bitcoin	$ 42,220.61	11.7%	56.9%	154.3%

Interest Rates

Interest rates are a powerful driver of economic activity and have a significant impact on financial markets. As inflation subsides, it seems ever more likely that the Federal Reserve "pause" in October signifies the

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peak in rates for this cycle. Although the high current level of rates can have a negative impact as they curb borrowing and business investment, the “pause” gives investors hope that rates will be lower in the future. The yield curve, meanwhile, remains flat and inverted as 2-year yields are higher than 10-year yields. This normally would indicate an economic slowdown is nearing, but coming off decades of historically low interest rates it could be that a normalization in underway. We anticipate a curve steepening toward the latter part of 2024 as the Fed begins rate cuts and a new economic cycle to be underway. The market seems to agree and is pricing in rate cuts as the Federal Reserve is set to begin easing its fight against inflation.

Economic Growth

Gross Domestic Product (GDP) is used to gauge economic activity in the U.S. by measuring the goods and services produced over a period. GDP rose 4.9% in the third quarter in 2023 and average GDP is expected to top 3% for all of 2023. This indicates a robust, expanding economy and shows how resilient our economy can be, in particular with consumers whose spending account for 2/3rd of all GDP. The strong labor market helps as the unemployment rate sits at just 3.7% which is historically low. Although GDP might stumble a bit out of the gates in 2024 as the effects of higher interest rates slow down parts of the economy, we expect that to reverse course in the latter part of the year as policy becomes more accommodative leading to more capital investment and increased borrowing and manufacturing.

The Bottom Line

It’s understandable that investors might be a little exuberant heading into 2024 following the market resurgence over the past couple of months. Yet they should be prepared for similar “up and down” periods just as in past years, especially with an uncertain election cycle approaching towards year-end. Still, despite all the uncertainty, the financial markets have been responding positively and moving higher expecting that the Fed has engineered a “soft-landing” and there will be continuing economic growth. With strong labor markets and a consumer base that has endured through past economic cycles and inflationary periods, we expect that if there is a slowdown in economic activity it will likely be short and shallow. As markets have become optimistic about the future, investors should have good reason to be optimistic as well.

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