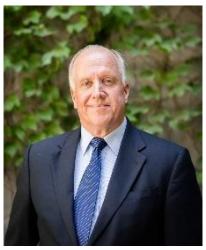
2023 – 4th Quarter Review & 2024 Outlook

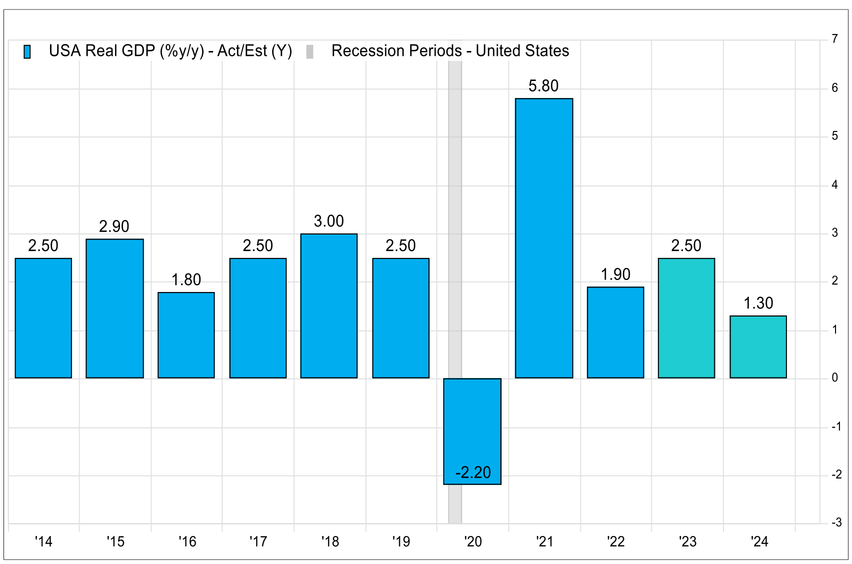
Economic and Investment Review



Mark Anderson

Chief Investment Officer

Economic Growth: Many economists forecasted a recession for some period of time in 2023; however, economic growth was significantly stronger in the U.S. than was anticipated prior to the beginning of the year. The consensus GDP estimate for 2023 was just 0.50% in December 2022 but expectations rose as the year progressed and GDP was



Source: FactSet

ultimately reported at a surprising 2.5% (advanced estimate). This compares favorably with the previous year's economic growth of 1.9%. Real GDP rose 3.3% annualized in the fourth quarter, well ahead of the consensus estimate of 2.0%, but down from 4.9% in the previous quarter.

Better than expected economic growth was largely the result of a resilient labor market and positively related consumer spending. It was anticipated that unemployment would move higher in response to the Fed raising interest rates. Higher interest rates have historically taken time to fully realize their impact on the economy and employment, but so far, the unemployment rate remains near historical lows at 3.7% in December.

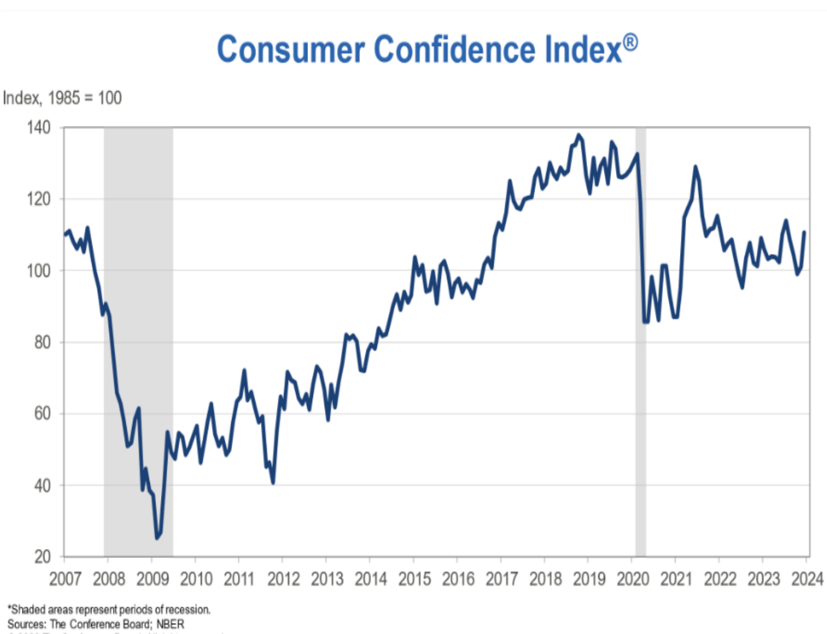
Recent headlines include tech companies increasing layoffs in an effort to improve efficiency prior to quarterly earnings announcements. Artificial Intelligence is getting some of the blame for displacing workers in some areas but AI demand is so great that it is having the opposite effect in other areas.

Consumer spending remained surprisingly strong during the year in the face of elevated inflation and interest rates. Retail sales were up 5.6% in December on a year-over-year basis. Two of the areas with the greatest increases in spending were in motor vehicles and food service.

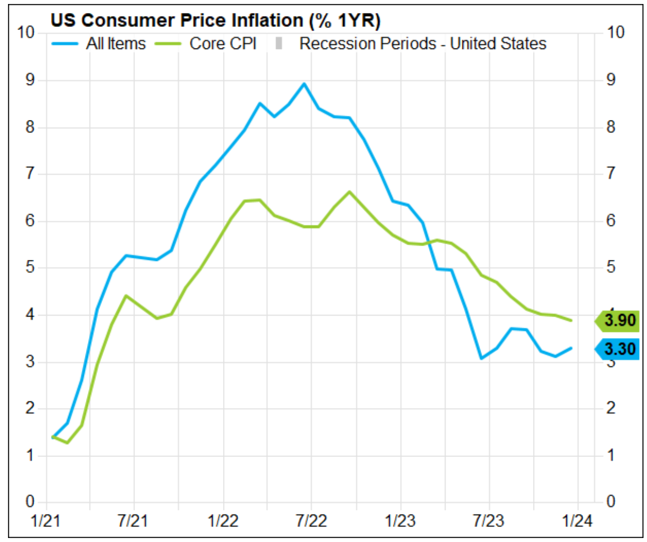
The economy was also supported by an increase in government spending, particularly at the state and local level. Businesses remained cautious due to higher interest rates, higher related costs, and the perceived potential for a recession.

Despite the stronger than expected economy in 2023, growth is expected to slow to 1.3% in 2024. Noted economist Mohamed El-Erian identifies a slowdown in consumer spending as a headwind to growth. He points to depleted pandemic-era savings and mounting household debt as reasons for the slowdown. Dr. David Kelly – Managing Director and Chief Global Strategist at JPMorgan Asset Management also expects consumer spending to grow more slowly but not shrink. He expects disposable income to continue to grow in 2024 but at a slower rate than in 2023.

The consumer confidence indicator provides a guide for future developments of households' consumption and saving. Dana Peterson, Chief Economist at The Conference Board, stated that December's increase in consumer confidence reflected more positive ratings of current business conditions and job availability, as well as less pessimistic views of business, labor market, and personal income prospects over the next six months."



Inflation as measured by the Consumer Price Index (CPI) declined from 8.0% in 2022 to 4.1% in 2023. On a monthly basis, inflation continued to trend down to 3.3% on a year-over-year basis in December. The consensus estimate for CPI in 2024 is 2.6%. The two largest contributors to the inflation rate currently are shelter and transportation services. The increase in shelter and transportation services costs are expected to level out in 2024 allowing inflation to move closer to the Fed's 2% target inflation rate by the end of the year.



Source: FactSet

A continued decline in inflation should result in the Fed having confidence to begin reducing short term interest rates. The currently inverted U.S. Treasury yield curve should transition to a flatter shape by the end of the year. Long-term rates may only move down marginally while short-term rates will likely move down markedly. The Fed expects that they will adjust the target rate down from a range of 5.25-5.50% to 3.75-4.00% by year-end. The market is betting on a faster rate of reduction.

GDP estimate revisions have been positive for the U.S. over the past six months. Estimates for the Emerging Markets ex-China have been picking up over the past three months while estimates continue to decline for Japan and Europe.

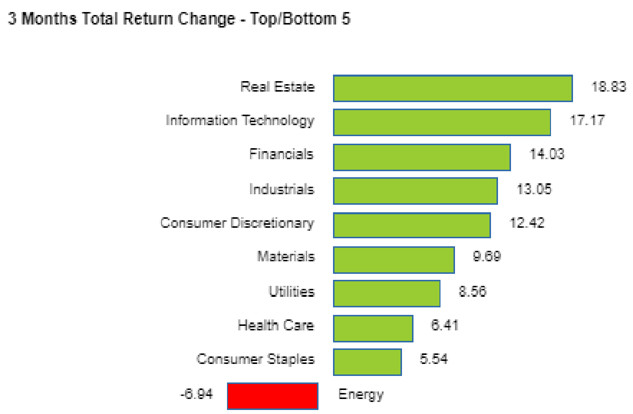
Equity Markets

Equity markets leaped higher in Q4 in response to lower inflation numbers and due to the perception that the Fed was done raising rates and that lower rates would soon be coming. The S&P 500 moved up 11.69% for the quarter and 26.29% for the year. Value stocks outpaced growth stocks in the quarter but growth stocks won the race for the year.

EQUITY	Q4 2023	YTD 12.21.23	1 Year 12.21.23	3 Years Annualized
S&P 500	11.69	26.29	26.29	10.00
S&P 500 Value	13.63	22.23	22.23	13.11
S&P 500 Growth	10.09	30.03	30.03	6.61
Dow Jones Ind Avg	13.09	16.18	16.18	9.38
NASDAQ Composite	13.79	44.64	44.64	6.05
S&P Mid Cap 400	11.67	16.44	16.44	8.09
S&P Small Cap 600	15.12	16.05	16.05	7.28
MSCI EAFE	10.42	18.24	18.24	4.02
MSCI Emerging Mkts	7.86	9.83	9.83	-5.08

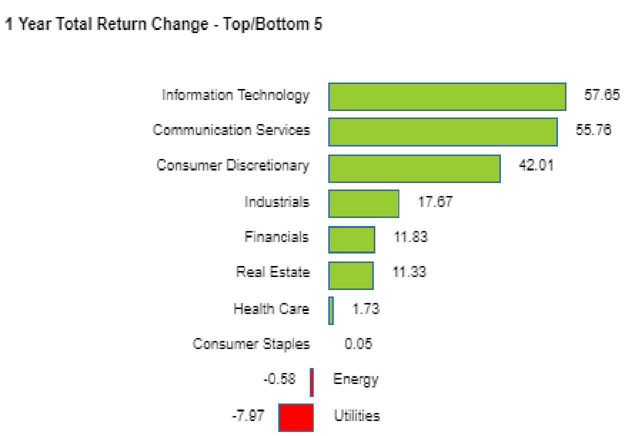
Source: FactSet

Every sector except Energy was positive in Q4. The strongest returns were in Real Estate and Information Technology.



Source: FactSet

Information Technology and Comunication Services lead the way for the year. Consumer Staples, Energy and Utilities were the laggards.



Source: FactSet

The tech heavy NASDAQ index was up 13.79% in the quarter and 44.64% for the year. The 10 largest stocks in the S&P 500 account for 32.1% of the index and were up 62% in 2023. The remaining 490 stocks were up just 8%. The Magnificent 7 stocks, comprised of Microsoft, Apple, Nvidia, Amazon, Alphabet, Meta and Tesla combine for 28.7% of the S&P 500 Index. Last year, the Magnificent Seven member stocks more than doubled, adding a combined $5.1 trillion in market value, according to Dow Jones Market Data.

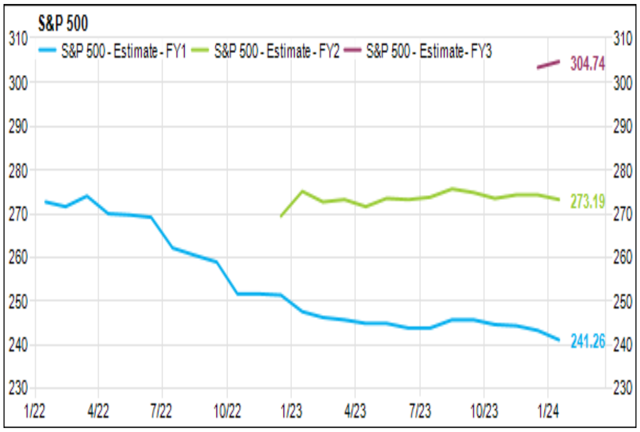
Small cap stocks lead the way in Q4 but continue to trail large cap stocks for longer periods. The S&P Small Cap 600 index was up 15.12% for the quarter and 16.05% for the year. Small cap stocks continue to trade at historically low valuation levels; however, the outlook for small cap stocks may be cloudy as economic growth is expected to slow. On the bright side, a diminishing potential for recession and the improved availability of credit should provide support.

Developed International stocks (MSCI EAFE) also participated in the upswing in the quarter and year. The international index continued to trail the S&P 500 but performed well, returning 10.42% in Q4 and 18.24% for the year. Valuations appear to be more reasonable than for the domestic large cap stocks, while at the same time, earnings growth looks to be comparative in 2024. However, a significant variance remains in the respective Technology sector weightings. The Technology sector accounts for just 10.6% of the EAFE benchmark versus 28.9% for the S&P 500.

Emerging market stocks (MSCI EM) continued to trail due to poor returns in China. The MSCI China benchmark was down -4.78% for the quarter and -10.60% for the year. Emerging markets ex-China performed much better. The related benchmark index moved up 13.03% in Q4 and 20.03% for the year. Valuations for the benchmark look stretched but earnings growth is expected to be strong over the next two years and may provide support.

Expectations for 2024 S&P 500 earnings growth have trended down slightly over the past few months but are still at lofty levels given the expectation for slow economic growth. The consensus forecast has adjusted down from about 12% to about 11%.

Expectations for strong earnings growth in the following years continues.



Source: FactSet

Goldman Sachs forecasts just 5.5% earnings growth for 2024. Raymond James expects earnings growth to be in the 2-3% range in 2024.

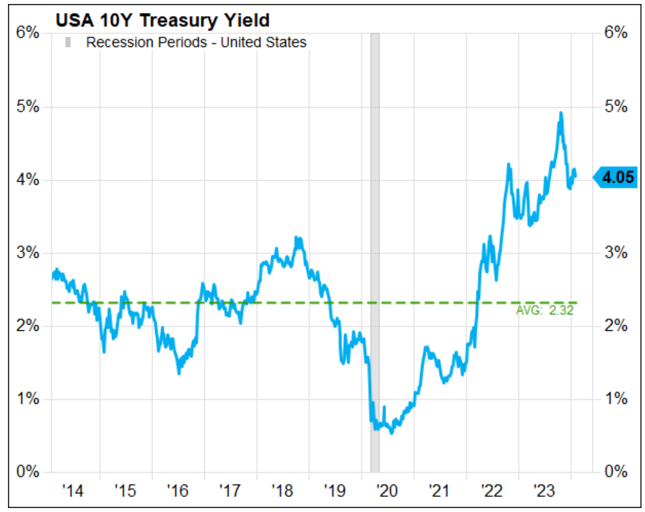
The S&P 500 is currently at 4,918 and is trading at 20.4x the 2024 consensus earnings estimate of 241.26 and 18.0x the 2025 estimate of 273.19.

We forecast the S&P 500 to be near 5,100 (up from our previous forecast of 4,900) by year-end 2024. The forecast is based on 9.9% earnings growth in 2024, compared with the consensus estimate of 11.3% and 11.2% earnings growth in 2025 compared with the consensus estimate of 13.2%. P/E multiples are forecasted to regress slowly towards the long-term mean but remain elevated due to the expectation for declining inflation and interest rates, strong EPS growth and increased AI efficiencies.

Goldman Sachs also forecasts that the S&P 500 will reach 5,100 by year end even with lower earnings growth expectations. Raymond James has a year-end target of 4,850 based on an ongoing potential for a recession and the lack of fear amongst investors. On the high side, Ed Yardeni, president of global strategy company Yardeni Research, forecasts the S&P 500 to reach 5,400 by year-end based on stronger that 2024 consensus earnings expectations and a list of improving economic data points.

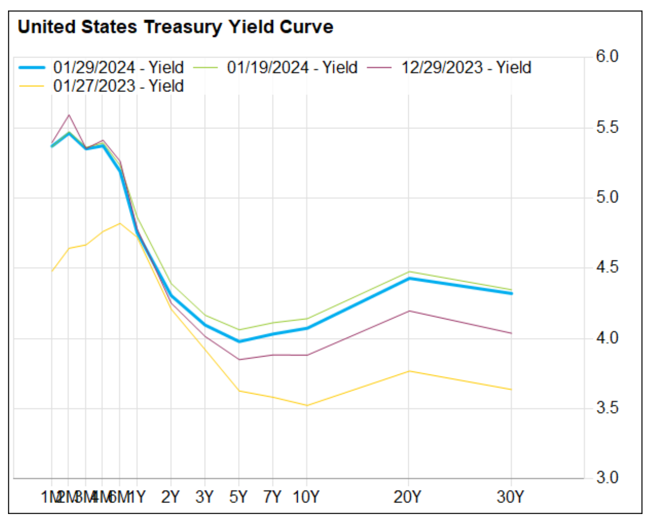
Fixed Income Markets

The 10-year U.S. Treasury yield reached the 5% level in October 2023. Interest rates have since moved lower but still remain considerably higher than the 10 year mean average.



Source: FactSet

The Treasury yield curve remains inverted with short-term rates higher than long-term rates, but the shape of the yield curve is expected to flatten out as



Source: FactSet

the Fed cuts rates during the year.

The year-end consensus estimate for the 10-year U.S. Treasury of 3.95% indicates an expectation for very little change from the current yield of 4.03%. The shorter-term rates will likely follow the Fed

Funds target rate lower when the Fed cuts rates. However, any cut in the Fed Funds rate may be delayed until there is further evidence that inflation continues to move lower.

The bond market rallied in Q4 as interest rates declined. The Bloomberg US Aggregate Bond Index rose 6.82% in the quarter and 5.53% for the year.

FIXED INCOME	Q4 2023	YTD 12.21.23	1 Year 12.21.23	3 Years Annualized
Bloomberg US Agg Bond	6.82	5.53	5.53	-3.31
ICE AMT-Free Nat'l Muni	7.06	5.93	5.93	-0.25
Markit iBoxx USD Liquid High Yield Index	7.21	12.89	12.89	1.73

Source: FactSet

Municipal bonds also followed the trend, returning 7.06% in Q4 and 5.93% in 2023. The spread between the yields for high yield bonds and Treasuries yields narrowed during the quarter as the prospect of a recession declined, allowing for attractive returns.

Following a terrible year in 2022, bonds have returned to their normal function of providing income and acting as an overall portfolio volatility manager.

Real Assets

Real Estate rebounded nicely in Q4. The Dow Jones U.S. Real Estate Index rose 18.0% in the quarter and as a result, finished the year well into positive territory.

Real Assets	Q4 2023	YTD 12.21.23	1 Year 12.21.23	3 Years Annualized
Dow Jones U.S. R/E	18.00	12.28	12.28	5.37
S&P GSCI	-10.73	-4.27	-4.27	19.18

Source: FactSet

Commodities, led lower by energy, moved down -10.73% in Q4 and -4.27% for the year.

Asset Allocation

We again reiterate that the opportunity should be taken to bring fixed income allocations to target due to higher yield opportunities and the likelihood that bond prices will respond positively to lower inflation in 2024. Money market and short maturity bonds remain attractive; however, as rates decline it may be advantageous to increase fixed income duration by moving farther out the yield curve.

Alternative investments can add value to diversified portfolios for investors with suitable risk tolerances, especially in the current environment. Additional income can be generated in private credit and attractive returns with lower volatility may be attained through private equity.

Disclosures