Thoughts from the Holy City

2023 The Year Behind & 2024 The Year Ahead

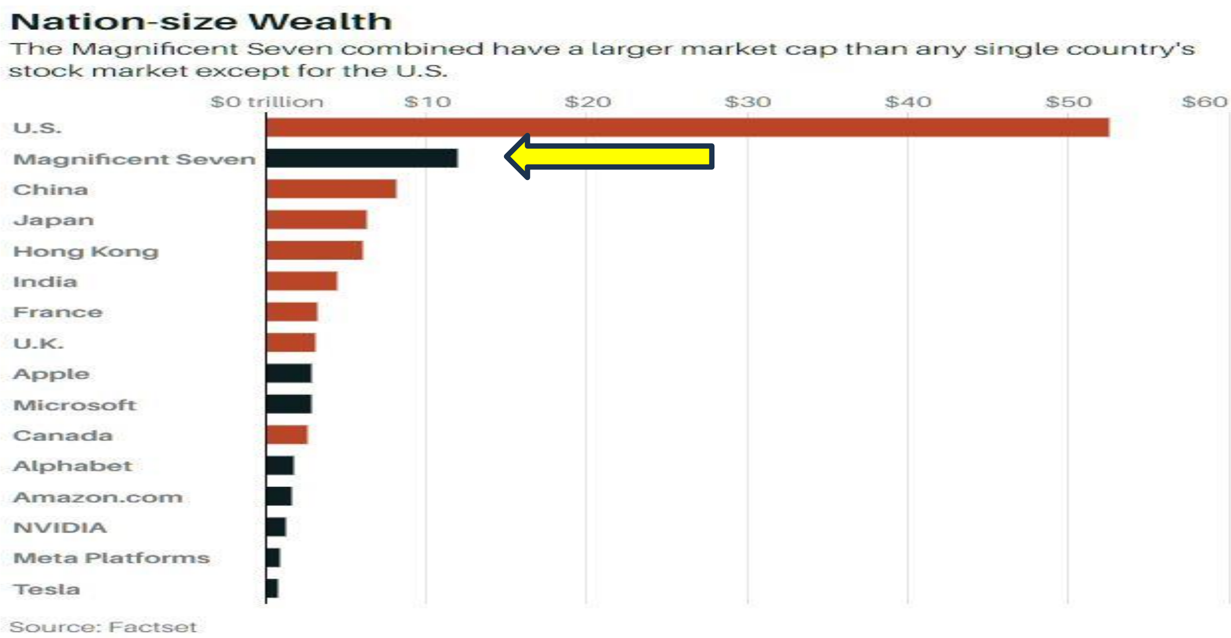
"True wealth is not measured by the amount of money in your bank account, but rather by the relationships you have, the impact you make, and the lives you touch."

~ Rich Roll

As we begin 2024, we kick off the year with our annual year ahead, year behind discussion. This is always a great opportunity to reflect on what transpired in the past year; revisit some of our predictions (be they right or wrong); and hopefully provide some insight into what may be in store for us in the coming year. I have been writing these annual reviews, as well as the monthly commentaries, for close to a decade now, and I always look forward to this one in particular. The past year turned out to be a year in which wealth management had the opportunity to thrive, and do so by actively stewarding client capital, and by not allowing the "noise" and behavioral finance to deter sound fundamentals and principles. It was the investors that sat on the sidelines, or those who attempted to time the market that suffered most.

2023: The Recession that Never Was

The year started off with quite a bit of negativity coming off a poor 2022. This is no surprise given that 2022 delivered a blow to investors in both fixed income and equites. Much of the sentiment with which we ended 2022 carried over into 2023 as the Fed embarked on one of the most aggressive rate hike campaigns in history, and it was widely expected they would steer us into a recession. By the end of January things were looking a bit better for the stock market, but it was seven stocks, also known as "the magnificent seven" that were pushing the market higher. This would be the case for the duration of the year. Although it can be tempting to try and chase returns of a handful of stocks in a year such *as the magnificent seven*, or *the FANG stocks*, *FAANG stocks*, or *MAMAA stocks,* the list goes on; more often than not, chasing returns leads to disappointment. These seven stocks alone make up nearly 28% of the market cap of the S&P 500, and the group alone are larger than any single country's stock market except that of the US. This is not feasible long term and will inevitably end poorly for those that chase these or any fad stocks.

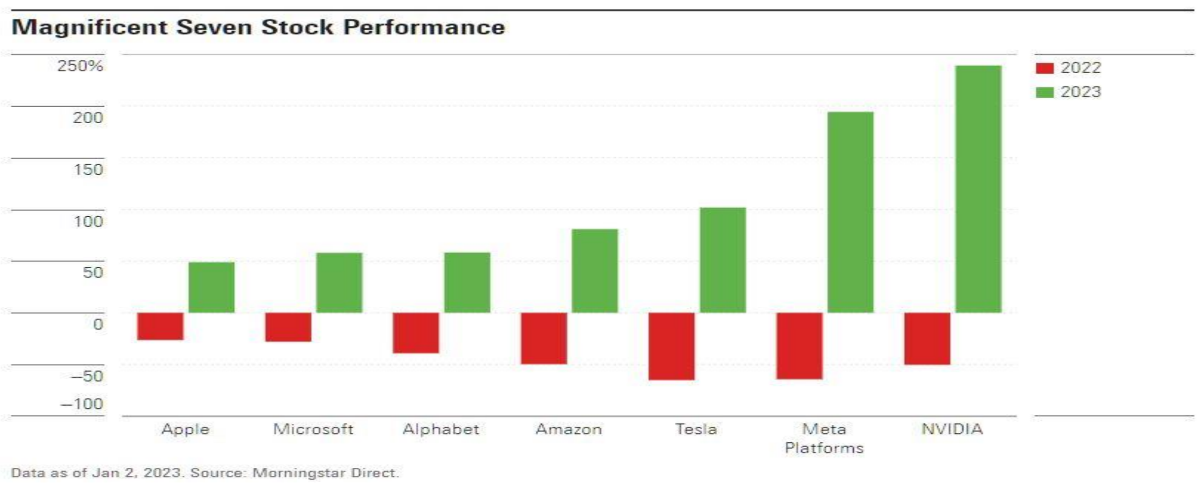


Then, in March there was a regional banking crisis as three regional banks, Silicon Valley Bank, Signature Bank of New York, and First Republic all went under. This appeared to be the so called "shoe to drop" that would be the demise of a good year. The Fed stepped in and ultimately backstopped the run on the banks preventing further contagion. Soon thereafter, concerns of Credit Suisse's underlying issues and long-term viability led to them being absorbed by UBS in a somewhat controversial takeover. One would believe that these events would be disastrous for the markets, but they were unphased.

There was continued speculation into the summer through Q3 & Q4, as uncertainty around what the Fed was going to do next. The largest drawdown of around 10% was in the later part of the third quarter, into the fourth as yields continued moving higher resulting in bond prices falling in tandem with the stock market. Then, the markets began to accept that we were not going to have a recession, the Fed held rates steady, and there was even discussion of rate cuts in 2024.

2023 ended up being a phenomenal year for investors, whether it was fixed income or equities, as pretty much all risk assets and asset classes ended the year in positive territory. That is not overly surprising given what took place in the markets in 2022. All this is despite pretty much every television pundit, economist, hedge fund manager, etc. calling for a recession in 2023, and quite a bit of volatility throughout the year; the said looming recession never materialized. The magnificent seven stocks would continue to push the market higher for the duration of the year. At one point the seven stocks accounted for nearly 100% of the return of the S&P 500, and despite the tide lifting all ships into the end of the year, 72 percent of companies still underperformed the index itself.

As is illustrated below, the market was very top heavy.



2024: A Look Ahead

As we look to the year ahead, it is safe to say that we are on the last leg of the post Covid 19 journey. There has been tremendous liquidity pumped into the financial system since the Great Financial Crisis, and subsequently during and after the pandemic. That, coupled with years of historically low interest rates, has made the environment very attractive for risk assets. It is safe to say that those days are behind us, but that does not mean that markets can't perform well; it just means it will be more of a grind than a glide. Inflation is still an issue, but it has dropped downward throughout 2023. There are both headwinds and tailwinds in store for 2024.

At the forefront of the discussion is the upcoming presidential election. Presidential election years always usher in uncertainty. It looks as though we will most likely be having a rematch of the 2020 election. There is great polarization in our country right now which will most likely lead to investors being cautious this year. Historically, during traditional presidential election years there are periods of weakness followed by rebounds as there is more clarity around key issues. In the United States the last sixteen Presidential re-election years have been positive for the stock market. The U.S. is one of over 60 countries electing a new head of state this year, representing nearly 49% of the global population, thus one of the biggest election years in history.

Although the U.S. election will certainly headline the year, the Fed, earnings, and market breadth are more likely to be the most important drivers of markets. As has been noted above, much of the 24% plus return of the S&P 500 came from seven stocks. There will need to be more breadth in the market for it to continue to rally in 2024, and we did see that trend begin in the last two months of the year. Historically since 1950, after 15%+ annual gains for the S&P 500, 93% of the time the subsequent years have been lower, with the average being around 9% (*1). Personally, I would prefer to see lower returns in 2024 so the market does not get too far ahead of itself, ultimately setting up for a significant pullback in 2025. Stocks are overbought and vulnerable to a pullback which we have already seen in the first few weeks of 2024.

Where do we go from here?

As we all know it is a futile attempt to try and predict the direction of the market and economy. There always have been, and always will be events that occur that derail the markets. Most of the time these are the so-called black swan events that no one could possibly forecast; the rise of the internet and the subsequent dot.com bubble, the September 11th terrorist attacks, Covid 19, etc. Human nature is to run (i.e. abort the plan and strategy in place), but this is one of the worst decisions an investor can make. The average annual peak to trough drawdown over the nearly past century is approximately 15%. Declines of about twice that have taken place with some irregularity every 5 years, but historically the market and economy always rebound. I have learned over my nearly 17 years in the wealth management business and a lifetime around it, that we must always revert back to the plan. I have built this business on what I believe to be a strong foundation of principles, disciplines, and processes around portfolio, risk, and behavioral management. There will always be doomsday scenarios, especially with the constant barrage of news that we face day in and day out. It is all about the process over the outcome. Don't focus on the end result, but rather concentrate on executing the game plan and the desired outcomes will follow.

I wish you all a prosperous 2024.

Be Well,

Grier

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Financial Advisor

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The S&P 500 is an unmanaged index of 500 widely held stocks.

The Magnificent Seven is a group of companies including Alphabet, Amazon, Apple, Meta Platforms, Microsoft, NVIDIA, and Tesla. Raymond James makes a market in these stocks. This is not a recommendation to purchase or sell the stocks of the companies mentioned.

Sources:

1. Raymond James Investment Strategy Quarterly. Volume 16. Issue 1. January 2024