Market Update – Q4 2023

MARKET UPDATE

The “Recession of 2023” that was widely forecasted failed to materialize this year. While economic data has remained favorable, there are signals that we are not out of the woods on recession. To name a few, leading indicators remain negative on a year-over-year basis; the unemployment rate, while still low, has moved above the 12-month moving average; and monetary policy remains in restrictive territory. However, rather than trying to time a recession, we advocate for constructing resilient portfolios as market volatility and recessions are a normal part of investing.

It was a “risk-on” market with most major asset classes posting favorable returns in the fourth quarter. Intermediate duration fixed income posted strong single digit gains, while many equity regions were in double digit territory. Much of the rally was fueled by the U.S. Federal Reserve’s (“the Fed”) shift to a more dovish tone and increased investor optimism about the possibility of a “soft landing” and the resulting significant interest rate move lower. Inflation continues to moderate, with U.S. CPI coming in at 3.1% in November 2023, moving toward the Fed’s target of 2%. We expect inflation to remain in a “messy middle” range of 2% to 5%. While the Fed remains “data dependent” we believe the current environment affords the central bank some room to pause or even ease if warranted.

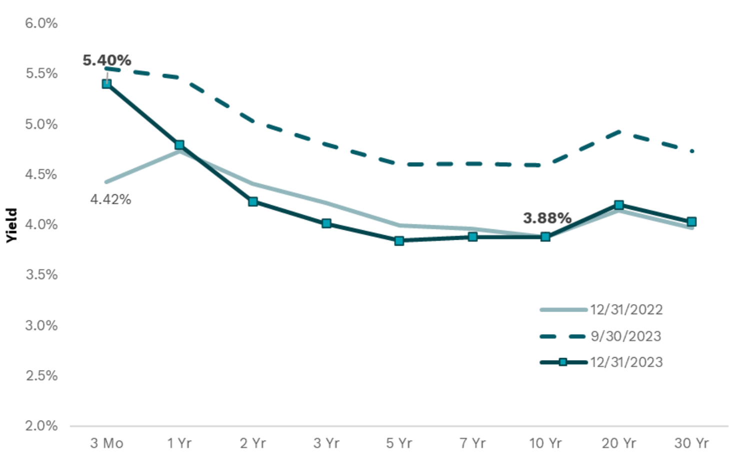
EQUITY

Equity markets were widely positive in the fourth quarter. U.S. small cap stocks (Russell 2000 Index) returned 14.0%, beating the large cap S&P 500 Index’s return of 12.0%. The prospect of lower interest rates in 2024 and the potential to shift out of the “higher for longer” environment helped fuel the small company segment. Valuations moved higher on the back of strong price movement this year; much of the move higher in U.S. large cap can be attributed to the “magnificent seven” stocks.

Non-U.S. equities also saw favorable returns. The MSCI EAFE Index (representing developed international markets) and the MSCI EM Index (representing emerging market equities) returned 10.4% and 7.9%, respectively. Europe experienced strong results, benefiting from moderating interest rates. Emerging markets lagged developed regions. While many emerging countries had positive results – such as Brazil, India, and Mexico – China, which accounts for a substantial portion of the EM index, fell 2.4% and was a main detractor. Equity valuations abroad also moved higher, but still look more attractive compared to domestic markets.

FIXED INCOME

The sharp move lower in interest rates buoyed bond prices in the fourth quarter. The Bloomberg U.S. Aggregate Bond Index gained 6.8% in the period and pushed the index’s 2023 return back into positive territory. The Federal Reserve held the Fed Funds rate steady throughout the quarter, targeting 5.25%-5.50%. The market began pricing in rate cuts in early 2024 as investors digested more dovish messaging from the central bank and inflation data moving closer to the Fed’s 2% target.



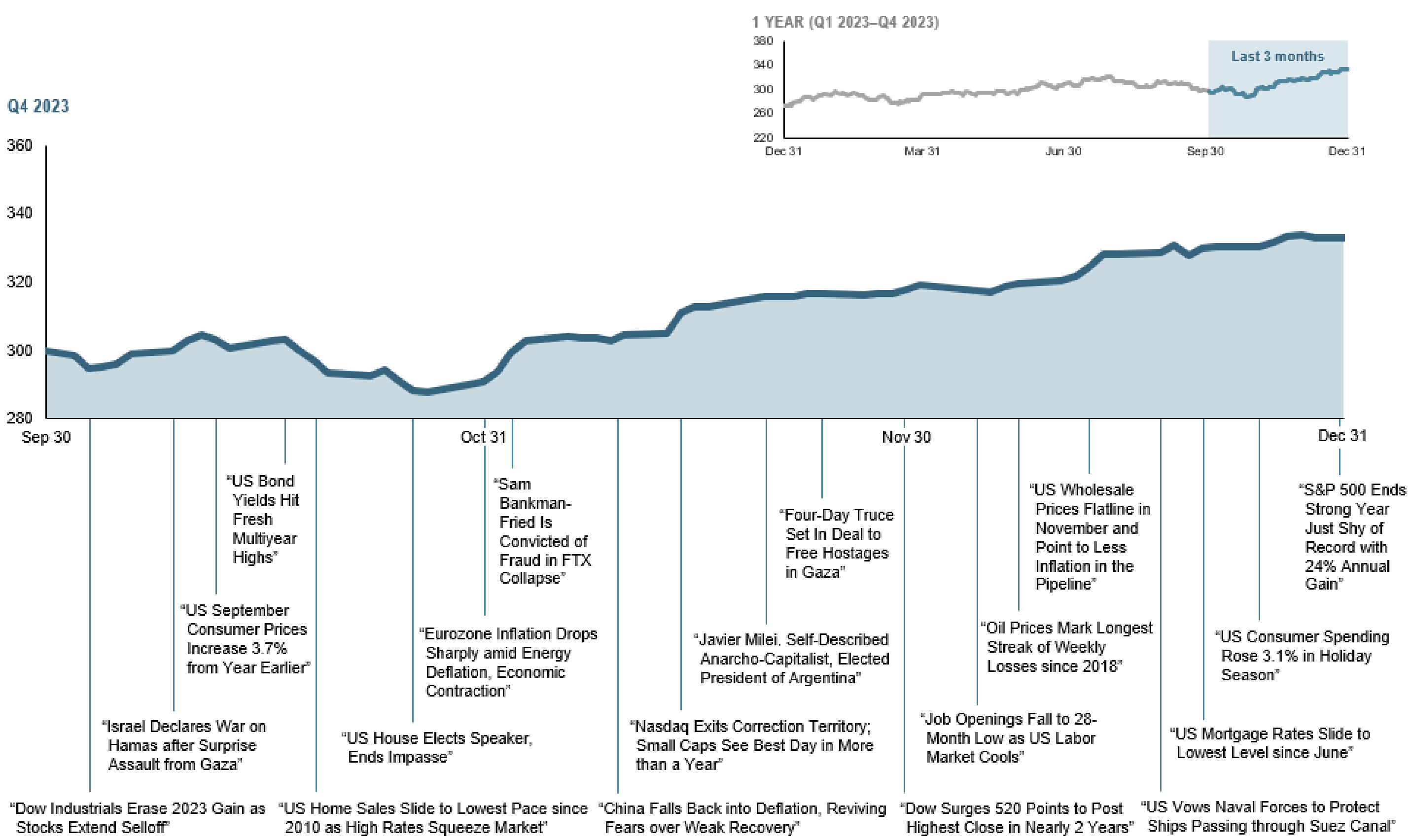
Corporate fundamentals remain favorable, helping to propel riskier segments of the fixed income market, such as high yield, past comparable government bonds. Credit spreads remain well below longer-term averages and are seemingly “priced for perfection.”

PERFORMANCE SNAPSHOT

	US Stock Market	International Developed Stocks	Emerging Market Stocks	Global Real Estate	US Bond Market	Global Bond Market ex-US
Q4 2023	12.07%	10.51%	7.86%	15.47%	6.82%	5.36%
YTD	25.96%	17.94%	9.83%	10.23%	5.53%	8.32%
1 Year	25.96%	17.94%	9.83%	10.23%	5.53%	8.32%
5 Year	15.16%	8.45%	3.68%	4.16%	1.10%	1.50%
10 Year	11.48%	4.32%	2.66%	4.72%	1.81%	2.80%

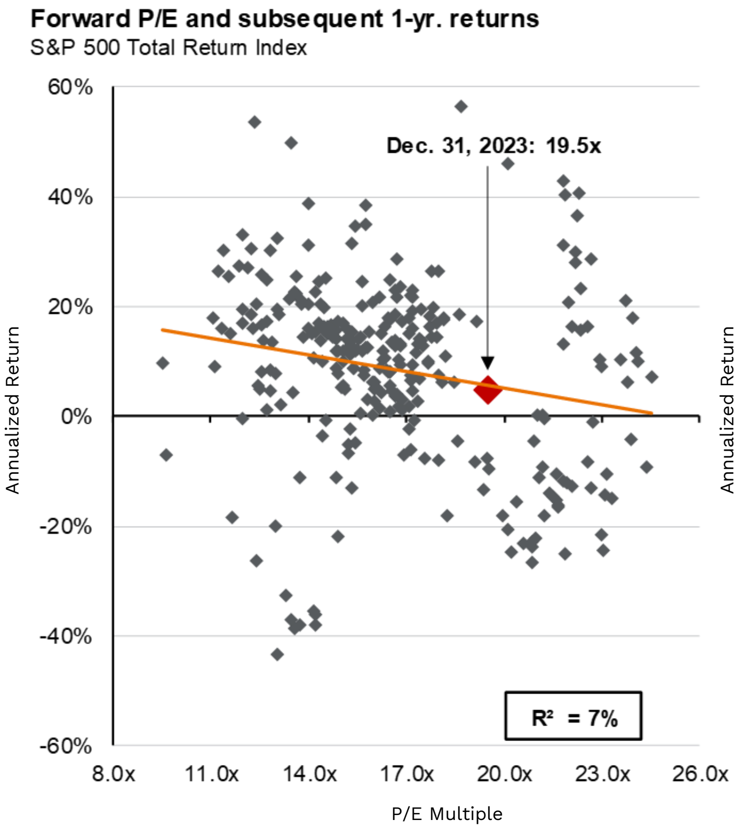
Index performance is provided as a benchmark. It is not illustrative of any particular investment. An investment cannot be made in an index. Past performance is not an indication of future results. Russell 3000 Index, MSCI World ex USA Index, MSCI Emerging Markets Index, S&P Global REIT Index, Bloomberg Aggregate Bond Index and Bloomberg Global Aggregate Bond Index ex-US. Returns as of 12/31/2023

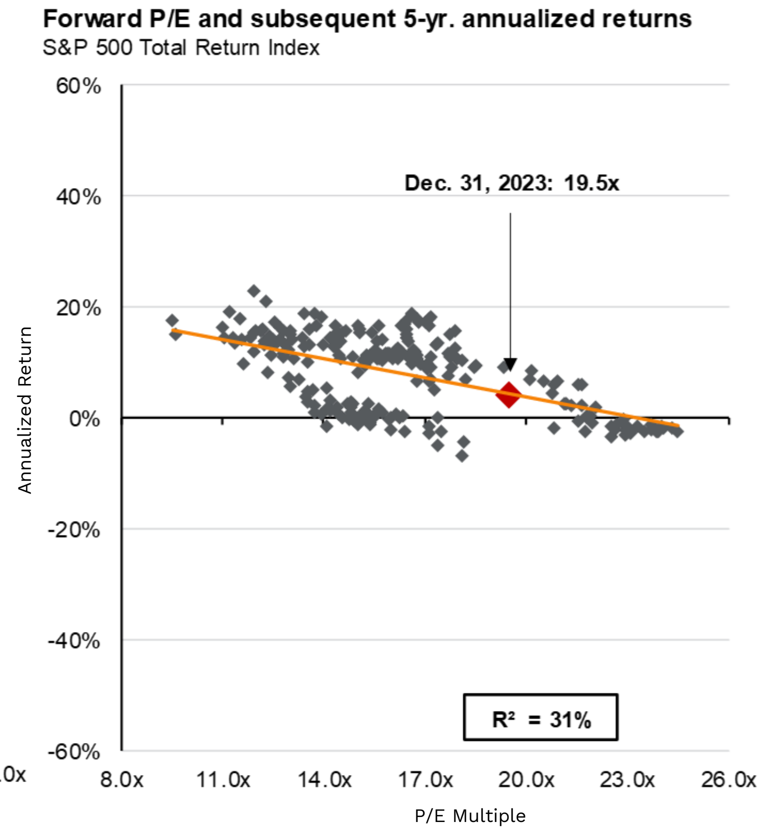
WORLD STOCK MARKET PERFORMANCE – Selected headlines from the past 3 months



These headlines are not offered to explain market returns. Instead, they serve as a reminder that investors should view daily events from a long-term perspective and avoid making investment decisions based solely on the news.

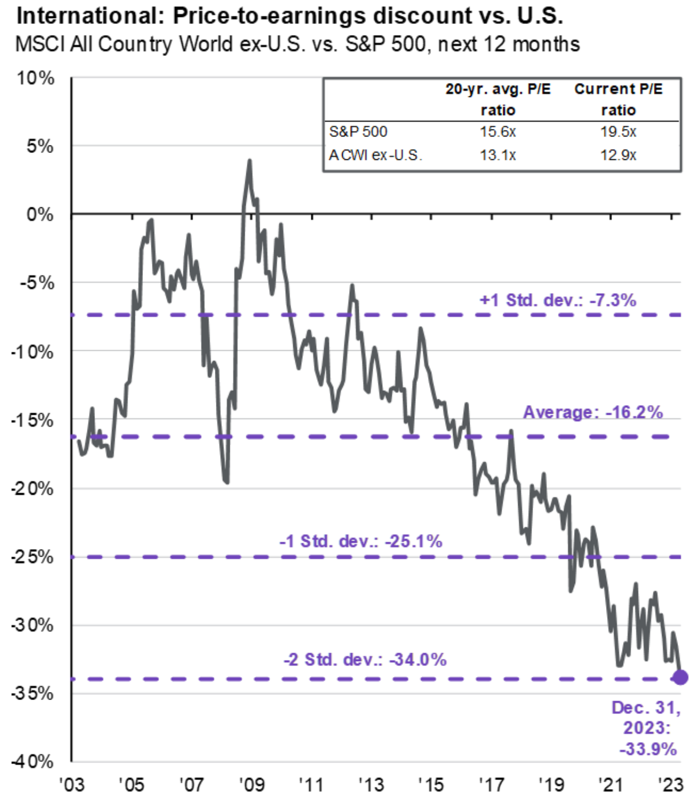
VALUATIONS MATTER – Short-term and longer-term outlook encouraging. At current valuations, the typical go-forward result is positive, especially over longer time periods.





Source: FactSet, Refinitiv Datastream, Standard & Poor's, Thomson Reuters, J.P. Morgan Asset Management. Returns are 12–month and 60-month annualized total returns, measured monthly, beginning 2/28/98. R^2 represents the percent of total variation in total returns that can be explained by forward price-to-earnings ratios. Price-to-earnings is price divided by consensus analyst estimates of earnings per share for the next 12 months as provided by IBES since January 1997 and by FactSet since January 2022. Guide to the Markets – U.S. Data are as of December 31st, 2023

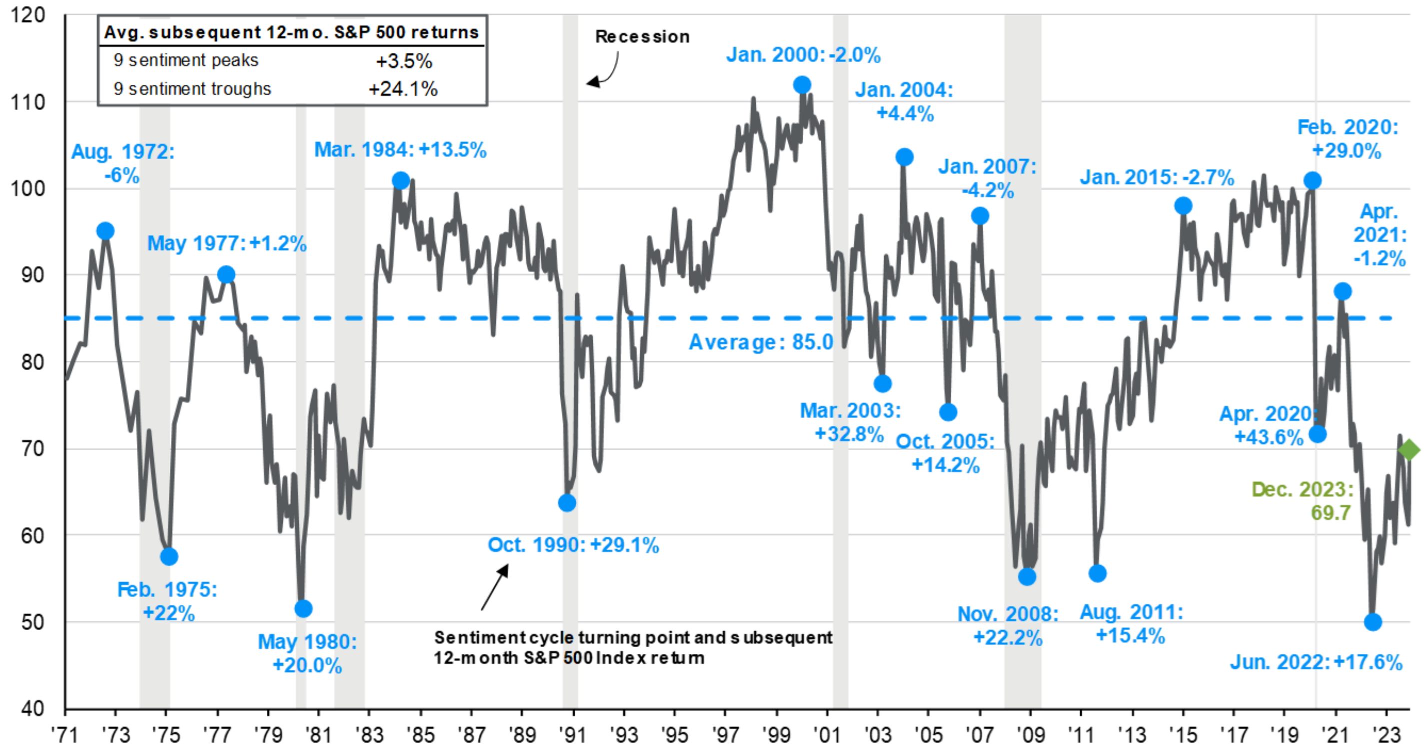
SCENARIO – Non-US markets are cheap relative to US Markets. That's been true for most of the past two decades. Not only are Non-US markets cheap relative to US Markets, but they are cheap relative to their historical discount to US markets. Moreover, at a 12.9x multiple they are trading below their long-term average while delivering a notably higher dividend yield. Couple this with a dovish shift in interest rate policy by the Fed (see Dollar trade lower) and you have a recipe to expect relative outperformance from the downtrodden equity segment.



Source: FactSet, MSCI, Standard & Poor's, J.P. Morgan Asset Management. Guide to the Markets – U.S. Data are as of December 31st, 2023

SCENARIO – Feeling gloomy about the go-forward? You are not alone. Fortunately, that general sentiment doesn't stay at these lower levels for very long. Moreover, the market returns subsequent to a trough in sentiment have been remarkably strong.

Consumer Sentiment Index and subsequent 12-month S&P 500 returns



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