With recession and inflation concerns sinking the equity markets during much of 2022, identical worries persisted well into 2023. The unexpected economic growth, strong corporate earnings and an increasing belief that a soft landing could be achieved set the stage for positive equity performance throughout the year. With the arrival of 2024, falling inflation around the globe continues beyond expectations, with core (excludes volatile food and energy) inflation rates nearing the Fed's target. The consensus points toward inflation running at the target rate of 2% for most developed economies. Household purchasing power should increase as a result. Tangled supply chains were a major factor (inflationary) in the Covid/ post Covid era. Wage pressure is subsiding. The trends that led to a highly inflationary period are unwinding, and should continue through 2024. With the Fed targeting 3 to 4 quarter point rate cuts this year, the market expectations for six seems wildly optimistic. Either way, a soft landing - which is difficult to accomplish - may be possible.

Equities defied all expectations in 2023, with the majority of prognosticators calling for recession early on. Justifiably so, with the Federal Reserve raising rates at the fastest pace since the 1980s/ a war in the middle east, an ongoing Russian invasion of Ukraine, and a regional banking crisis all played into a decelerating scenario. Throughout the year, equities headed higher, being interspersed with periodic aggressive moves lower. A textbook example of why market timing generally does not work well. Taking the long term view will alleviate the thought that one can outperform market returns by selling aggressively when all is looking bleak, to repurchase at even lower prices, or conversely selling when all is optimistic - with the expectation that the market has to be overvalued. It is a complicated science. Seemingly unlimited variables constitute the inputs to corporate earnings, economic output and consumer spending/ sentiment. Perhaps someday AI will have a predictive model that gets close. A perfect predictive model would end the viability of the equity market concept. Equities with perfect predictability would become similar to a fixed income instrument.

One area of concern for the near term, in my view, is the increasing debt levels for the American consumer. Most alarming, credit card debt surpassed $1.08 trillion in 3Q23. Total household debt (all sources) at the end of 3Q23 tallied $17.29 trillion. To make a bad situation worse, the rapid rise is occurring at a time of increasing interest rates. Credit card revolving debt is rapidly taking more purchasing power away from those who can least afford the loss. Unable to pay off the monthly balance, a large percentage of the population is relying on credit cards for essentials, while another segment is simply spending beyond their means. While there are some signs of a return to more normal levels over the next year, the trend cannot be ignored. A strong consumer is driving much of the growth - all while consumer sentiment is relatively low. If indeed there is no reversal, the trend is non-sustainable. While not often referenced as the fuel for increased consumer spending, credit card debt is and will be a precarious funding mechanism for many. Will monitor quarterly debt statistics as released by the Federal Reserve.

2024 will in all likelihood provide slower growth, coupled with lower inflation, and reduced consumer spending. This mix holds the ingredients that will allow for a soft landing scenario. The fed will be lowering rates, perhaps aggressively, around the middle of the year. As rates fall, expect a pickup in residential real estate activity. The commercial real estate segment will in general continue to experience a decline, with some possibility of recovery in the latter part of 2024. Large investments from the CHIPS Act/ Infrastructure Bill and Inflation Reduction Act have paved the way for an unprecedented surge in manufacturing construction. Large productivity boosts from AI may start to surface in economic statistics. With declining rates, it makes sense to replace short term money market rates with longer dated fixed income with 2 to 4 year duration. Please call or email anytime. Risk/ reward will provide for a multitude of shifting scenarios as we move through the year that impact the allocation between cash/ stocks and bonds and how a portfolio should be structured. Thank you. All the best for 2024 and beyond!

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