MacDougall
Financial Counseling
2364 Route 66 Delmont, PA 15626
www.macdougallfinancial.com

Dear Clients of MacDougall Financial, January 16 , 2024

> *It was the best of times, it was the worst of times, it was the age of wisdom, it was the age of foolishness, it was the epoch of belief, it was the epoch of incredulity, it was the season of Light, it was the season of Darkness, it was the spring of hope, it was the winter of despair…Charles Dickens, 1859- Tale of Two Cities*

One of the recurring themes in the Tale of Two Cities is that 'things are not always as they seem' and 2023 proved that in spades! You could not ignore the burgeoning global wars, the dysfunctions of most democracies, and the return to the 'old normal' of real interest rates. It was a year for the contrarians for rarely have forecasts been so wrong. Nearly all pundits expected a recession, especially in corporate profits and real estate, but all sectors remained strong. Housing has not collapsed and supply chains are improving. Inflation has been the one bright spot in the sea of statistics falling from 7-9% late last year to circa 2-4% today. High interest rates, an inverted yield curve, and near full employment were to be the harbingers of bad times; but so far, for reasons yet to be fully divined, we have achieved significantly higher interest rates without crushing the stock market, labor market, nor the economy.

Despite a dysfunctional Congress, a few bank failures, and rising war and debt service costs, the stock market averages had a banner year. The S&P 500 rose 24% but about half of the gains came in the magnificent 7 stocks and 2/3rd's (330) of these 500 stocks returned less than the index! This concentration of returns and the lack of 'breadth' has resulted in a wide dispersion of returns as exemplified by the NASDAQ 43% rise to the 13.7% DOW increase. Looked at another way, the top 10 S&P 500 stocks returned circa 62% while the remaining 490 stocks returned 8%! The 4th quarter witnessed a broadening of the base and strong rallies in both stocks and bonds. The dispersion of returns is also evident in the sector results, which ran from a high of 57.8% in tech to a low of -7.1% in utilities. Seven of eleven sectors showed solid double digits gains (12-55%) whereas four sectors were flat to negative.

After a disastrous 2022, the bond markets were quiet/flat in the first half of the year. The 10 year benchmark T-bill rate basically opened and closed flat on the year at 3.8%. However, there was a steep run up in rates in Q3 and subsequent fall in Q4, which helped most bond funds to achieve a 2% to 5% annualized return. The Barclays AGG index closed up 5.5%, reversing a 6% decline as of mid-October! Truly the 4th quarter decline in interest rates made the year for bond managers. Quarterly GDP growth remained positive throughout the year, which was not in the forecasts. The Consumer's health and willingness to spend has been a welcome surprise and is driven by changes in the post-pandemic labor markets and the sizable fiscal largesse. Increases in average hourly earnings (due in part to minimum wage increases in 25 states) are above most measures of inflation, indicating real wage gains. Wages lagged inflation in recent years so there is ground to be made up. Job openings continue to outnumber 'job seekers' by a large margin. Real estate underpins most consumer balance sheets and the post-pandemic valuation increases are holding. In most markets, the housing inventory for sale is the problem, not demand, even with high rates.

Oil markets were mostly calm during the past year with prices falling approx. 10%. Gas is under $3 per gallon in many states providing relief for consumers. The US continues to be one of the dominant players at 13.3MM bpd with only Saudi Arabia producing more. OPEC's market share globally hit 50% and continues to decline. Guyana is the new "Alaska" with over 11 billion barrels of estimated reserves. This has revived a territorial dispute with Venezuela and a conflict is brewing. Speaking of foreign markets, Greece was the surprise winner two years in a row in a list of 35 OECD countries with modest inflation, rising employment, and as the IMF said "increasing market competition". Their stock market rose 40% in 2023 despite 'fiscal austerity' (Greek oxymoron). The USA came in third on this list using 5 different criteria. It is noteworthy that many of the other

top ranked countries were in the Americas (Canada, Chile, Mexico) and many of the laggards are in northern Europe (Germany, Sweden, Finland). Overall, nearly all OECD countries showed respectable positive GDP growth, tight labor markets, and moderating inflationary pressures over the course of 2023.

Looking at the performance of your mutual funds is a reminder why staying invested is wise. After a veritable flood of negative returns in 2022 and with all forecasters predicting only more doom and gloom, 2023 witnessed mostly positive returns in the solid double digit category (+12% to +40%). Growth again bested value and our small cap funds roared back with 15-30% returns. Even international funds, long our laggard, sported decent double digit returns excepting those with a China focus. Chinese stocks fared badly mostly due to the increasingly heavy hand of the government reigning in the internet tycoons. The worst sectors were health care, consumer staples, energy, and utilities, which is probably a good buy list for 2024! Fundamentally, the lesson of 2023 was to not change your investment plans based on forecasts. No one can foresee the future, better to set an 'all weather' strategy that allows you to sleep well.

At present, most see "sunny days" for 2024 but please recall that when there is a consensus, approach with caution. Wars, elections, and a fragile global economy will definitely produce surprises. Europe and China face structural issues of declining populations, high energy costs, and strained public finances. Defaults in some of the highly indebted countries will probably occur. There might be a 'tail wind' of declining interest rates through the year and moderate growth but neither are guaranteed. Countervailing pressures from the bond vigilantes and radical proposals from either the right (balance the budget), or the left (eliminate fossil fuels), will only serve to destabilize the markets. "Uncertainty" and "Unprecedented" will be the 2024 media catchphrases for the "times are a'changing". A 'rolling recession' cannot be ruled out.

On the plus side, America is self-sufficient in energy, food, and the consumer has purchasing power. Generous transfer payments plus wage gains have driven an increase of 3.3MM jobs in the Jan-Nov 2023 time period. Most household balance sheets are strong with both financial and real assets gaining substantial value in the years between the Great Financial Crisis (GFC 2008-10) and the Great Pandemic Crisis (2020-23). Inflation and the many Wars are the wildcards for 2024…and beyond. However, we have seen the broad inflation numbers decline and both goods and services supply chains are normalizing. Onshoring, nearshoring, and infrastructure will underpin a high level of capital investments. It is in the International arena that we see the greatest pitfalls and rewards. Is our political system able to articulate a coherent foreign policy in the face of rapidly changing situations? Flexibility and unity will be required and those attributes don't spring to mind when discussing Congress and our political parties. They, like the many College Presidents and public unions, claim to be listening but are clearly not hearing.

Forecasts are in fact mixed for 2024 with Goldman and BofA predicting 6-12% S&P 500 growth and JP Morgan forecasting a 8-10% decline. JPM has the most 'cute' 2024 forecast of 2% GDP growth, 0% recession chances, 2% inflation, and 4% unemployment…..2024!!! Volatility measured by the VIX fell through most of 2023 so it is a safe bet it will rise over the coming 12 months. Adding to volatility will be the elections scheduled in over 50 countries representing more than 50% of the world's population with highly unpredictable outcomes. Taiwan just happened, to China's displeasure, and it is only the beginning.

Diversification and low costs are our 'touchstones' and I will close with the best words of advice that I have seen in a while: "Hope for the Best, Prepare for the Worst, and Get on with Life". Liberally translated this says: "Keep most of your funds in equities, hold enough cash and 'safe' assets to cover 2-4 years of spending, and smell the roses."

Please call or email us with any questions for we are here to help you achieve these simple goals.

Advisors to Individuals and Families - Phone: 724-468-1300; Fax: 724-468-1301