Third Quarter 2023 Update

October 12, 2023

The third quarter of 2023 closed with a change in direction for the market. The first half of the year presented investors with an upward trend, but the most recent quarter exhibited its normal seasonal weakness.

Over the last 50+ years, August and September have been the worst performing months (on average), with September being the only month with a negative average return. The S&P 500 ended down 3.3% for the quarter but remains up 13.1% year-to-date.

It appears we are in another market phase where returns are led by just a handful of the largest stocks. This time around the benchmarks have been driven by the "Magnificent 7," as they are termed, consisting of Nvidia, Meta (Facebook), Tesla, Amazon, Alphabet (Google), Microsoft and Apple. These seven stocks alone have a 27% weighting in the market-cap-weighted S&P 500 and their outsized effect on the index is illustrated by the fact that the equal-weighted S&P 500 Index is only up 1.8% year-to-date.

A lot of the reason for these stocks' outperformance has been the public awareness of Artificial Intelligence and its potential impact to the economy and to individuals' lives.

Outside the "Magnificent 7", the energy sector seemed to be the only shining star in the quarter primarily due to surging oil prices. Amid a rise in WTI (West Texas Intermediate) to over $90 per barrel, precipitated by extended supply cuts by OPEC and Russia, consumers and companies have pulled back, which lessens the probability of a soft landing for the U.S. economy.

A housing slowdown, labor strikes in the auto industry, plus the resumption of student loan payments, means that a fair amount of economic stimulation has disappeared.

Federal Reserve policy has also dominated the headlines of the third quarter. Current expectations are that we can expect one more 0.25% increase this year, but expectations for 2024 are that we will see two rate cuts versus the original expectation of four, which reiterates the Fed's theme that rates will likely be higher for a longer period than the markets had expected.

While changing economic conditions can stimulate debate and cloud short-term prospects, it does not alter our long-term strategy of seeking to invest in strong companies, run by sound management teams at reasonable prices. We'll keep up the search and do our best to discount the noise.

One final thought that we would like to make with this letter is to reiterate our opinion that it is okay to take capital gains in your taxable stock portfolio. The cost of this is, of course, the 20% capital gains tax, but you keep 80% of that gain – and you give yourself the opportunity to reduce your portfolio's overall risk level or invest in what may be a better long-term performing company. Most importantly, you may increase your ability to get a good night's sleep.

As always, we welcome a discussion of your portfolio, financial needs or just the opportunity to visit with you. We are grateful for your business and trust. Feel free to contact us any time.

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