Mosaicfi *Market Insights*

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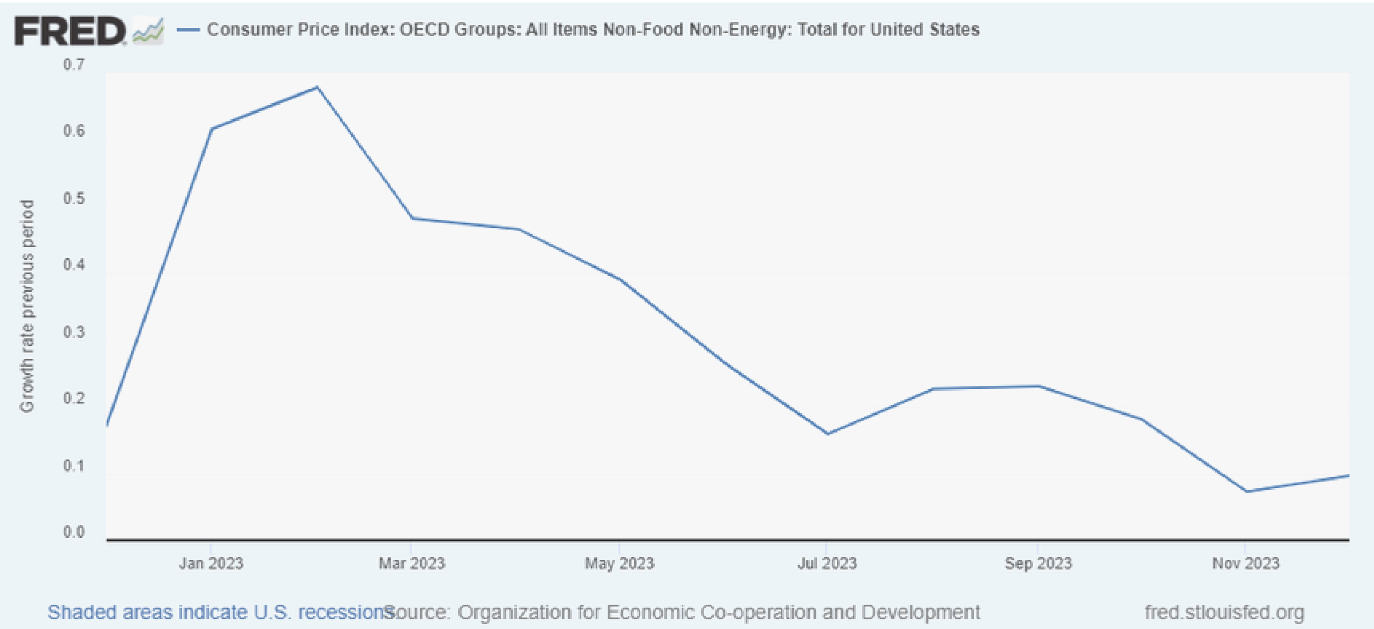

Q4 2023

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Finally… we can do what my yoga instructor tells me to do over and over… breathe.

The 4th quarter finally gave us what we have been waiting for these past couple of years - lower inflation. This set off a relief rally in both the equity and bond markets. Not only did inflation continue to recede, but employment remained strong.

It appears that the Federal Reserve managed to pull off what many have questioned - a soft-landing. This refers to the Fed raising interest rates high enough to slow down economic growth with the goal of taming inflation; but not so much that it throws the economy into a recession. We don't know what 2024 will bring, but as we closed out 2023 the soft-landing camp seems to be winning.

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It is quite remarkable that, after experiencing a spike in inflation to a degree that we have not seen in decades, over a relatively short period of time, the Federal Reserve was able to contain it through the monetary policy tools available to them. Especially when you consider the behavioral psychology around inflation. It can become a self-fulfilling prophecy; if you expect higher prices, you demand higher wages, which causes employers to charge higher prices, and so on and so on. This can be a difficult cycle to break, which is why investor fear is so strong when there are concerns about inflation.

THE EQUITY MARKETS

Global equity markets, as measured by the MSCI All Country World Index, were up 11.42% in the 4th quarter and up 23.79% for all of 2023. In Q4 the international developed equity markets underperformed the US equity markets. International developed markets were up 10.51% vs. the U.S. equity markets, which were up 12.07%. For the full year the international developed markets were up 17.94% vs. the US which was up 25.96%. Emerging markets underperformed developed markets for the quarter. EM was up 7.86% in the 4th quarter and on a one-year basis was up 9.83%. After underperforming the rest of the markets for most of 2023, US REITs had a very strong quarter, up 16.35% for the quarter and up 13.96% for the year.

Large cap stocks again underperformed small cap stocks in the US for the 4th quarter. Small cap stocks were up 14.03% vs. large cap stocks which were up 11.96%. But for all of 2023 large caps were up 26.53% vs. 16.93% for small cap stocks. In a reversal from 2022, large cap growth stocks significantly outperformed value stocks with growth up 42.68% vs. 11.46% for value for all of 2023.

THE FIXED INCOME MARKETS

With the positive news in the 4th quarter on the inflation front, interest rates declined, reversing the relentless march higher that we experienced for most of 2023. The yield on the 10-year Treasury declined by 71 bps over the quarter. This was great news for the bond market. The performance of the overall market was up a whopping 6.82% in the 4th quarter and ended the year in positive territory, up 5.53% overall. The municipal bond market outperformed the taxable market for both the quarter and for all of 2023; muni bonds were up 7.89% for the quarter and up 6.40% for the year.

The high-yield market once again had strong performance, up 7.16% for the quarter and ended the year up 13.44%. US TIPS (inflation protected securities) were up 4.71% for the quarter and were up 3.90% for the year.

So, what did all this mean for investors?

Depending on the asset allocation, a diversified portfolio was up somewhere between 8-10% for the 4th quarter and up between 11-16% for all of 2023.

LOOKING AHEAD

While inflation appears to be contained and the march to higher interest rates behind us, the Federal Reserve will not feel compelled to begin lowering interest rates as long as the unemployment rate remains at historical lows.

As we have written about before, the Fed's dual mandate is 'to achieve maximum employment and keep prices stable'. Nowhere in there does it state that it should target a certain level of economic growth; that is not its concern. It lost sight of this over the past couple of decades when inflation remained low and there was no apparent cause for concern. The Fed will not make that same mistake again.

There are a lot of things for the markets to digest in 2024; a US presidential election, an on-going battle in Washington over spending and keeping the government running, two wars being fought, etc.

While these are issues and concerns that we all read about and think about, rarely do events such as these have a significant longer-term impact on market performance.

We certainly want to understand the implications of geo-political events, but it is always important to remember that reacting to shorter-term events from a portfolio management standpoint can take you off your long-term trajectory.

As always, we would love to hear from you, so feel free to contact us at any time.

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