Investment Report Q42023

The last quarter of 2023 saw an incredible turnaround in the markets following the declining inflation, strong economic growth, and an unexpectedly dovish Federal Reserve decision. Both equities and bonds mounted a strong rally in the last two months of the year, following a challenging start to the fourth quarter. The acceleration was caused by robust economic growth in the third quarter, better inflation data, and the cessation of Federal Reserve (Fed) rate increases. This led to a sharp increase in stock prices and the S&P 500 reaching levels not seen in more than two years, yielding the best annual return since 2021.

The fact that equities and bonds were under a lot of pressure at the beginning of the fourth quarter is somewhat hidden by the great performance throughout the quarter. First, as in the third quarter, Treasury rates continued their upward trend in early October, which put pressure on stocks and bonds. Then, the market was a surge in oil prices because to expectations that Israel, Hamas, Lebanon, and possibly Iran might go to war in the region. As investors priced in a potential oil-driven rebound in inflation, higher oil prices drove a subsequent increase in Treasury yields. These elements, along with a lacklustre earnings season, caused the 10-year Treasury yield to hit 5.00% for the first time since the mid-2000s, and the S&P 500 to drop to its lowest points since mid-May. But when Fed Governor Chris Waller hinted that rate hikes were done and that rate reduction might occur in 2024, the markets went the other way. The market responded positively right after, with bonds and stocks rallying strongly until the end of the month to close well above the lows and with only a 2% fall.

<u>Fourth Quarter Performance Review</u>

All four of the major U.S. stock indices reported robust quarterly gains during the fourth quarter, which saw a broad and robust surge in stocks. The Russell 2000 and Nasdaq 100 outpaced the S&P 500 over the previous three months, indicating that investors' expectations for rate reduction in 2024 had a significant impact on markets in the fourth quarter. Companies in those two indices are anticipated to benefit most from a sustained decline in interest rates. Over the course of the year, however, the tech-heavy Nasdaq 100 significantly outperformed the other major stock indices, rising more than 50%, driven by the combined effects of 1) Artificial Intelligence (AI) euphoria and 2) Rate cut predictions.

The S&P 500 experienced a noteworthy increase of more than 20%, primarily attributable to the index's high weighting of technology stocks. While still seeing tremendous profits in 2023, the less tech-sensitive Dow Industrials and Russell 2000 outperformed the Nasdaq and S&P 500. Remarkably, the index performance for the entire year 2023 was the exact opposite of what happened in 2022, when the Dow Jones Industrial Average and S&P 500 suffered a decrease that was significantly greater than that of the Nasdaq and small caps.

Because smaller companies usually benefit more from lower rates, small caps beat large caps in the fourth quarter based on market capitalization thanks to those increasing rate drop predictions. However, due to the strength of large-cap tech stocks and the fact that small cap performance was negatively impacted by higher rates in the first three quarters of 2023, large caps beat small caps for the entire year. Growth substantially beat value in terms of investment strategy throughout the fourth quarter and the entire year. The causes were well-known: Early in 2023, growth funds with a strong tech focus were driven by the excitement around artificial intelligence, and growth equities were expected to benefit from rate cuts in the fourth quarter. The opposite of 2022, when value outpaced growth due to rising rates and recession fears, is also true today: growth outpacing value.

At the sector level, eight of the eleven S&P 500 sectors concluded 2023 in positive territory, while 10 of the 11 sectors concluded the fourth quarter with a positive return. Unsurprisingly, sector trade in the fourth quarter and all year was driven by anticipation for rate drops as well as the combined effects of artificial intelligence enthusiasm. Expected lower rates had a significant impact in the fourth quarter, as REITs and tech were the two best-performing industries. As interest rates decline, both will gain. In addition, cyclical sectors have performed well over the last three months as the Fed's hint of further rate decreases has raised hopes for steady economic growth. However, over the course of the entire year, the three most "AI sensitive" sectors (tech, consumer discretionary, and communications services) greatly outperformed the other eight S&P 500 sectors, indicating that AI enthusiasm was the dominant force in sector trading.

While higher rates (for the majority of 2023) decreased demand for high dividend yielding sectors, defensive sectors—such as consumer staples and utilities—lagged in the fourth quarter and overall year as economic growth proved to be more resilient than anticipated. After being the greatest relative performers in 2022, consumer staples and utilities showed negative returns in 2023.

S&P 500 Total Returns by Month in 2023											
Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec
6.28%	-2.44%	3.67%	1.56%	0.43%	6.61%	3.21%	-1.59%	-4.77%	-2.10%	9.13%	4.54%

Source: Morningstar

US Equity Indexes	Q4 Return	2023 Return
S&P 500	11.69%	26.29%
DJ Industrial Average	13.09%	16.18%
NASDAQ 100	14.60%	55.13%
S&P MidCap 400	11.67%	16.44%
Russell 2000	14.03%	16.93%

Source: YCharts

Globally, foreign markets underperformed the S&P 500 in the last quarter of 2023, primarily due to weaker-than-expected gains in developing markets as a result of heightened geopolitical tensions in the Middle East and persistently weak economic development in China. Due to better-than-expected inflation data and growing hopes that other major central banks will follow the Fed's example and lower rates in 2024, foreign developed markets outperformed emerging markets in Q4. Foreign developed markets saw strong returns for the entire year 2023, but they significantly outperformed the S&P 500, largely because of the significant increases in U.S. tech stocks.

International Equity Indexes	Q4 Return	2023 Return
MSCI EAFE TR USD (Foreign Developed)	10.47%	18.85%
MSCI EM TR USD (Emerging Markets)	7.93%	10.27%
MSCI ACWI Ex USA TR USD (Foreign Dev & EM)	9.82%	16.21%

Source: YCharts

Commodities

2023 will see persistently high global inflation. The crisis in Ukraine, price hikes for commodities, and, in certain regions of globally, the persisting strength of the US currency are going to trigger shortages in the supply chain that will continue to push yearly inflation well beyond 2019 levels. In the agricultural sector, falling prices for sugar, cotton, corn, and Kansas wheat were not countered by rising prices for coffee, cocoa, soybeans, and wheat. Lead and nickel prices in the industrial metals market decreased during the quarter, but those of zinc, copper, and aluminium increased. Silver and gold, two precious commodities, had significant price increases during the quarter. Despite a strong rise in gold, commodities saw a broad decrease in the fourth quarter due to weakness in oil, which was caused by growing concerns about global economic growth and a reduction in geopolitical risks. Early in December, gold reached a new all-time high as a result of a rise in the value of the US dollar. Commodity demand forecasts were dampened by worries about economic development, particularly from China and portions of Europe, which resulted in somewhat negative returns for commodities in 2023. Nonetheless, the fourth quarter dollar decrease helped gold end the year with a healthy positive return.

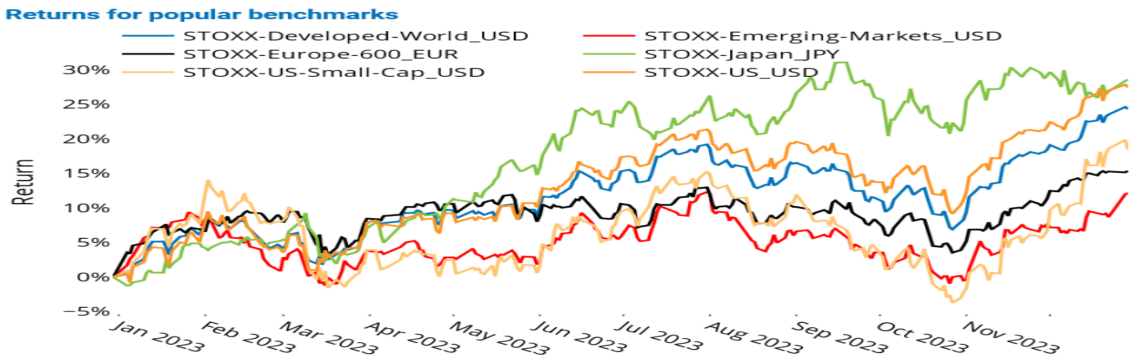
Commodity Indexes	Q4 Return	2023 Return
S&P GSCI (Broad-Based Commodities)	-10.73%	-4.27%
S&P GSCI Crude Oil	-21.29%	-11.17%
GLD Gold Price	11.55%	13.11%

Source: YCharts/Koyfin.com

Emerging markets

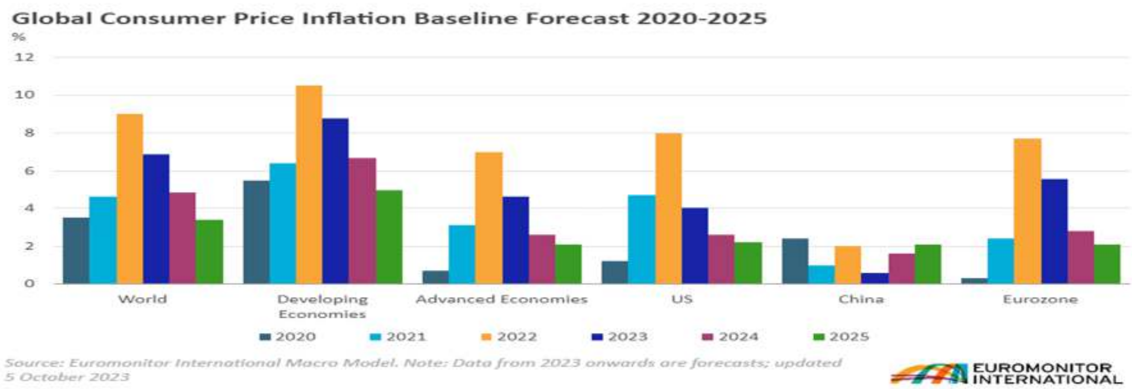
Even though gains were erratic throughout the year, 2023 ended well for most markets. Japan led for the majority of the year, but the US had a great December and Japan had a slight negative return, meaning that for the entire year, the two nations were tied. The Developed World index saw a return of more than 20% thanks to these two markets. Developed Markets ex-US performed better than the US market in the first half of the year, but since May, as equities have continued to rise, the US market has been beating the ex-US market. Up until December, when they surged by more than 11%, US small-cap equities significantly underperformed their large-cap counterparts. Despite still trailing Large Caps for the year, US Small Caps finished ahead of Europe and Emerging Markets thanks to favourable tailwinds. With the election of Donald Tusk as prime minister and the head of a pro-EU liberal coalition government, which ends the eight-year dominance of the populist Law & Justice (PiS) party, Poland was the best-performing country over the quarter. In US currency, Mexico, Egypt, and Peru all had impressive double-digit returns. The central bank's subsequent cut in policy rates, along with persistent signals of disinflation, was the main driver of Brazil's outperformance. Thanks to the substantial returns from some tech-related firms and the continued strength of tech exports, Taiwan outperformed the EM index. Korea also saw a surge in support due to its tech-related performance. Greece, Hungary, Colombia, and South Africa were also up, with the latter being helped by a reduction in blackouts (also known as "load shedding"). India saw significant gains in the context of declining inflation and a dominant performance by the ruling Bharatiya Janata Party in significant state elections. In contrast, China's return was negative due to growing fears about its economy. As per Axioma Equity Risk Monitors tracks only a few other regions, and Asia Pacific excluding Japan is the only one that ended the year in the red.

Despite wild inflation, growing interest rates, a banking crisis, and an agitated geopolitical landscape (with at least two ongoing wars, Russia-Ukraine and Israel-Hamas, both of which had the potential to spread to other areas at some point), the world economy appeared to be resilient. Indeed, morale did improve, especially in the fourth quarter, as hopes that the Fed and other central banks would halt rate hikes and possibly even cut them in order to prevent a sharp decline in value were stoked.

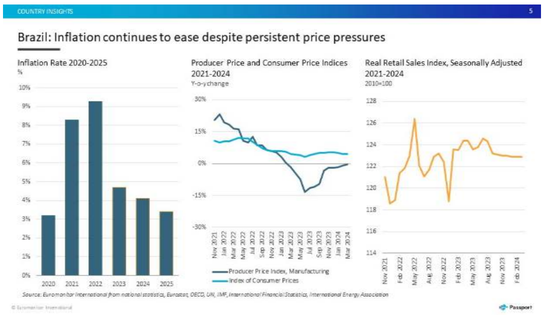


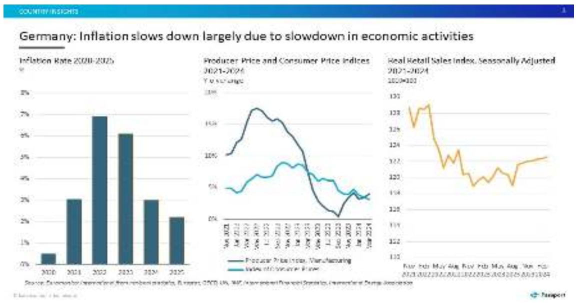
Global inflation

The US Consumer Price Index fell from 6.5% at the beginning of the year to 3.4% in December 2023, indicating a fall in inflation in the fourth quarter. Progress was aided by a sharp fall in the price of energy, a decline in the price of new and used cars, and a moderating cost of food. Since shelter costs have only now begun to decline, 2024 should see even more improvement. During October 2023, in 28 OECD nations, there were decreases in inflation between the third and fourth quarters of 2023. In contrast, Greece, the Czech Republic, and Costa Rica saw increases in inflation of at least one percentage point. Denmark saw nearly zero inflation, the Netherlands saw negative inflation, and Costa Rica saw negative inflation despite increases. After a slowdown earlier in 2023, consumption increased at a strong rate of 2.8% in Q4. The consumption of goods and services during the fourth quarter drove spending growth, which was bolstered by a 2.5% increase in real disposable income compared to the previous quarter's 0.3%. If this pattern holds through 2024, the growth in consumer spending may become more sustainable. On the other hand, there should be caution given the recent increase in household debt levels and poor savings.



The inflation rate for China has been revised down to 0.6% in the fourth quarter of 2023 and is predicted to rise to 1.6% in 2024. Weak economic growth and private expenditure continue to constrain price increases. The deflationary climate raises the likelihood of further government involvement, which is expected to increase consumer confidence in 2024. The stabilization of energy costs has contributed significantly to the reduction of inflation concerns throughout the eurozone; yet, national differences still exist. Germany and France, the two biggest economies in the eurozone, are expected to see 3.0% and 2.6% of inflation, respectively, in 2024. However, given that government actions in 2022 served to defer the unfavourable consequences of rising oil prices, France is probably going to see delayed inflationary effects. Brazil's inflation rate peaked in 2023 at 4.7% and continued to decline to 4.1% in 2024





Bonds

Turning now to the fixed income markets, the major benchmark for bonds, the Bloomberg Barclays US Aggregate Bond Index, saw positive returns in both the fourth quarter and the entire year due to lowering inflation and rising bond prices as a result of anticipated rate cuts in 2024. If we go deeper into the fixed income markets, we find that in the fourth quarter, longer-duration bonds beat shorter-duration bonds as bond investors priced in future reductions in Federal Reserve interest rates in response to lower-than-expected inflation. However, for the entire year, shorter-duration notes beat longer-term bonds due to the long end of the yield curve being burdened by strong inflation readings over the first three quarters of 2024.

Regarding the corporate bond market, investors embraced the notion of lower interest rates and fewer possibilities of a recession, as seen by the sharply positive returns generated by both high yield and investment grade bonds for the fourth quarter. Due to the robust economy encouraging investors to take on more risk in exchange for a higher yield, high yield corporate bonds beat investment grade corporate debt for the whole year.

US Bond Indexes	Q4 Return	2023 Return
BBgBarc US Agg Bond	6.82%	5.53%
BBgBarc US T-Bill 1-3 Mon	1.38%	5.14%
ICE US T-Bond 7-10 Year	6.42%	3.38%
BBgBarc US MBS (Mortgage-backed)	7.48%	5.05%
BBgBarc Municipal	7.89%	6.40%
BBgBarc US Corporate Invest Grade	8.50%	8.52%
BBgBarc US Corporate High Yield	7.16%	13.44%

Source: YCharts

The stock and bond markets had tremendous gains in the last two months of 2023, rising by around 15% and 8%, respectively. The equities and bond markets saw year-to-date returns of 25% and 5%, respectively, thanks to these increases. It is important to remember that these recoveries came after large sell-offs that occurred in both markets a few months earlier. Also, as per the Bloomberg Global Aggregate indices, the fixed income markets had their best quarterly performance in more than two decades during the year's last quarter. This performance was primarily caused by a perceived change in the direction of monetary policy, from a "higher-for-longer" posture to potential rate reductions. The yield on government bonds dropped precipitously, while the credit markets surged and outperformed government bonds. The market rise was accelerated by the US Federal Reserve's (Fed) far more obvious shift to a more dovish tone in December, despite the Fed maintaining rates unchanged during the quarter. Three rate decreases are now predicted for 2024, up from the previous two, according to the updated dot plot, a chart that plots Federal Open Market Committee (FOMC) estimates for the federal funds rate. More positive news on PCE inflation, the Fed's most closely monitored indicator, suggests that the FOMC is more confident in the work being made in bringing inflation back on track. As markets anticipated easing conditions, rates on government bonds decreased generally. By the end of Q4, the yield on the US 10-year Treasury had dropped from 4.57% at the end of Q3. The German 10-year Bund yield finished the quarter 0.81% lower at 2.03%, while the UK 10-year gilt yield dropped from 4.44% to 3.54%.

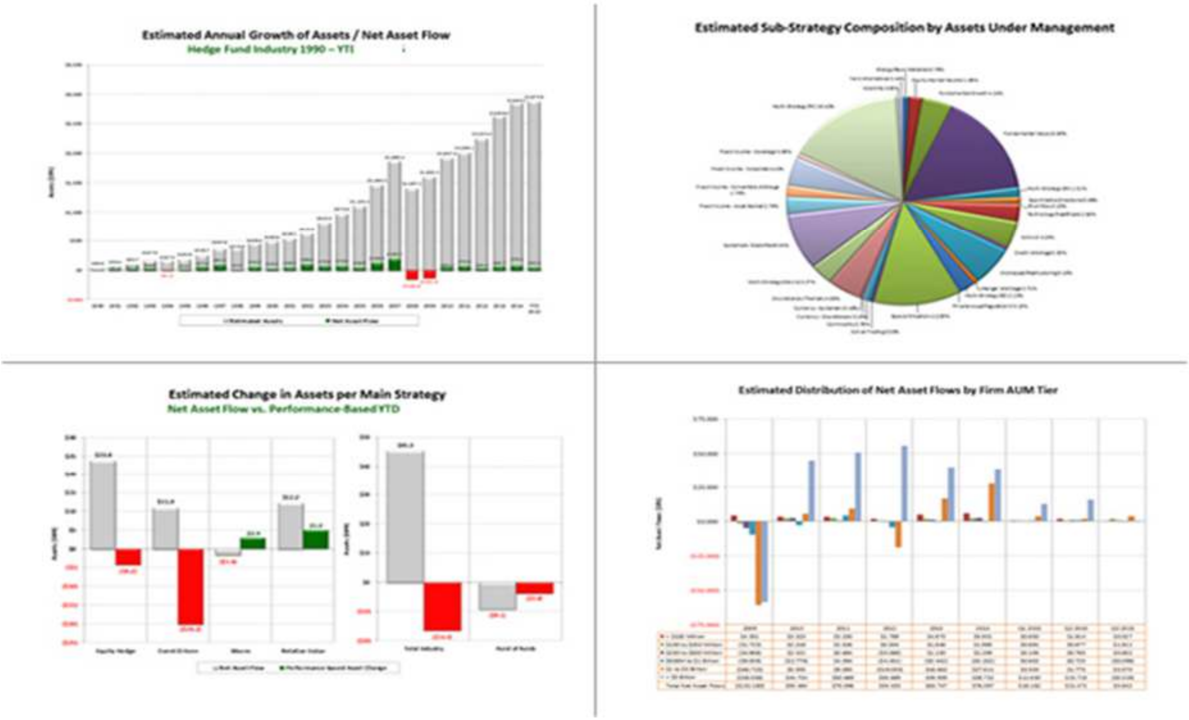
	3 months			12 months		
Government bonds	**USD**	**EUR**	**GBP**	**USD**	**EUR**	**GBP**
JPM GBI US All Mats	5.6	1.2	1.1	4.3	0.7	-1.6
JPM GBI UK All Mats	13.2	8.5	8.4	10.0	6.2	3.8
JPM GBI Japan All Mats**	6.8	2.4	2.3	-6.0	-9.2	-11.3
JPM GBI Germany All Traded	10.8	6.2	6.1	9.1	5.4	3.0
Corporate bonds	**USD**	**EUR**	**GBP**	**USD**	**EUR**	**GBP**
BofA ML Global Broad Market Corporate	8.7	4.1	4.0	9.5	5.8	3.3
BofA ML US Corporate Master	7.9	3.4	3.3	8.4	4.7	2.3
BofA ML EMU Corporate ex T1 (5–10Y)	12.2	7.5	7.4	13.9	10.0	7.4
BofA ML £ Non-Gilts	12.1	7.5	7.4	15.1	11.2	8.6
Non-investment grade bonds	**USD**	**EUR**	**GBP**	**USD**	**EUR**	**GBP**
BofA ML Global High Yield	7.6	3.2	3.0	13.4	9.6	7.0
BofA ML Euro High Yield	4.3	0.0	-0.1	3.5	0.0	-2.3

Source: LSEG DataStream. Local currency returns in Q4 2023: *2.0%, **0.9%.

Hedge funds

According to information released by HFR in the most recent edition of the HFR Global Hedge Fund Industry Report, total hedge fund assets climbed for the fifth consecutive quarter in 4Q 2023, reaching an estimated $4.11 trillion, or a quarterly increase of approximately $112 billion. Strong performance-based gains and a $24.5 billion net outflow from investors in uncorrelated macro strategies during the fourth quarter drove the expansion in hedge fund capital. As of the start of last quarter of 2023, the aggregate assets under management (AUM) for Asian hedge funds and emerging markets remained stable. The directional Equity Hedge and Event-Driven strategies drove the HFRI Fund Weighted Composite Index's +7.6 %gain in 2023. Gains were also driven by exposure to Technology/AI and the late-year acceleration of M&A, both of which are projected to continue through early 2024. The HFR Cryptocurrency

Index increased by +37.8 % in the fourth quarter, bringing its return for FY 2023 to +65.2 %. The projected AUM for emerging markets was $245.8 billion, while the total capital invested in Asian hedge funds was $126.6 billion. The HFRI Macro (Total) Index fell -0.6% in 2023 as a result of uncorrelated macro strategies, which saw mixed results from fundamental and quantitative strategies. With net asset withdrawals of $12.2 billion for the quarter included, total macro capital decreased by an estimated $22.4 billion in 4Q, bringing total macro strategy capital down to $670.5 billion. Systematic Diversified CTA strategies, which track trends and are quantitative, saw the largest declines in macro sub-strategy asset values in the fourth quarter, falling by an estimated $16.6 billion. The HFRI Macro: Discretionary Thematic Index led the divergent 2023 Macro sub-strategy performance, rising by +4.8% year over year, while the HFRI Macro: Systematic Diversified Index led the falls, falling by -3.9%.



Performance Across Regions

Eurozone

With hopes that there might not be any more interest rate increases, the last quarter of the year saw great performance for eurozone shares. The MSCI EMU index saw a 7.8% increase. The two biggest laggards, with negative returns, were healthcare and energy, while the top-gaining sectors were information technology and real estate. Softer inflation data from the US and the eurozone encouraged investors to buy shares, suggesting that interest rates may have peaked and that cuts may be imminent in 2024. Annual inflation in the euro region decreased from 2.9% in October to 2.4% in November. The annual rate of inflation was 10.1% a year ago. The economy of the eurozone has been impacted by higher interest rates. Third-quarter GDP in the Eurozone decreased by 0.1%, according to Eurostat figures. In December, the HCOB flash purchasing managers' index (PMI) for the eurozone dropped to 47.0. This implies that the economy of the area most likely shrank in Q4 as well. The manufacturing and services sectors' survey data serves as the foundation for the PMI indices. A reading of 50 or higher implies expansion, while one below 50 denotes contraction.

UK

Throughout the quarter, UK equities increased. Due to the high performance of domestically focused firms, UK small and mid-cap indices beat the overall market. This happened as expectations that interest rates may have peaked grew, and foreign offers for smaller UK enterprises were continuing to increase. Particularly in the financial and industrial sectors, some of the market's more sizable, internationally exposed, and economically sensitive segments fared well as well. However, larger corporations were often held back by sterling's strong performance relative to the weak US dollar. Over the period, UK inflation decreased more than anticipated; in November, the consumer prices index fell to 3.9%, according to the Office for National Statistics (ONS).

US

With hopes that interest rate reduction may be on the horizon, US shares market saw significant gains in the last quarter of the year. The S&P 500 index fell short of its all-time high, which was reached in the first few months of 2022. Over the period, the US consumer price index (CPI) experienced a slowdown, going from 3.7% in September to 3.2% in October and 3.1% in November. The core personal consumption expenditure index, the preferred inflation gauge used by the Federal Reserve (Fed), increased 0.1% month over month in November, which was less than anticipated. In the meantime, rate of economic growth was revised down to 4.9%. The statistics supported market forecasts that the Fed will begin cutting rates in 2024 after concluding its cycle of rate hikes. The Federal Open Market Committee's most recent policy meeting minutes revealed that officials anticipate interest rates to conclude the year between 4.5% and 4.75%, down from the current range of 5.25%. The most interest rate-sensitive industries, such as consumer discretionary, real estate, and information technology, were also the best performing. Because of the quarter-over-quarter decline in crude oil prices, the energy sector saw a negative return.to 5.5%.

As 2024 starts to unfold, the market's prognosis is extremely promising. Rate cuts are imminent, most likely in early 2024, and the Fed is done raising rates. The economy has grown more robustly than most people could have predicted, and worries of a recession have mostly subsided. The Fed's goal inflation rate was not far from being reached in 2023, and corporate earnings growth is predicted to pick back up in the upcoming year.