

FLAGSTONE

FINANCIAL ADVISORS, INC.

MARKET REVIEW CALENDAR YEAR 2023

What Happened:

A year ago, an overwhelming majority of financial analysts were forecasting a dismal year for stocks in 2023. Boy, did they get that wrong. The markets had a stellar year in 2023 with many major stock indices hitting new highs. The S&P 500 index barely missed a new top, but still returned an impressive 26%. Buoyed by enthusiasm over AI (artificial intelligence), a group of stocks known as the Magnificent Seven—Amazon, Alphabet, Apple, Microsoft, Nvidia, Meta and Tesla—had collective gains of 107%. Small cap stocks and international stocks also shined with impressive returns of 17% and 18%, respectively. As the year wore on, the red-hot market drew in more and more investors from the sidelines which spurred even more stock advances.

How did so many experts get this wrong? We suspect it was due to the sour mood lingering after the 2022 bear market. Few saw a reason for the market to improve. However, our firm took a closer look and what we saw suggested that the worst was behind us. Economic indicators were flashing positive signals that the economy was not in terrible shape. To wit, we had exceptionally low unemployment—the lowest since 1969. Inflation was slowing and corporate earnings were growing. In short, there was light at the end of the tunnel.

The bond market also saw significant changes in 2023. After many years of record low interest rates, rates climbed to new highs in response to the Fed's efforts to combat inflation by raising interest rates. By October, 10-year Treasury bond yields had risen to about 5% and mortgage rates ballooned to 8%. This rise was painful for those looking to finance a home or a car purchase. But investors, especially retirees, welcomed the higher rates. Fixed income and money market investments were viable asset classes again after years of near-zero rates. Rates have fallen somewhat from the October highs, but it is very unlikely that they will drop to the near-zero rates of the past few years.

2023 Calendar Year Performance:

S&P 500 Index (large stocks)	26.3%
Russell 2000 Index (small stocks)	16.9%
MSCI EAFE Index (international stocks)	18.2%
Bloomberg U.S. Aggregate Bond Index (bonds)	5.5%

Prognosis:

2023 was a great year for the financial markets. History tells us that good years usually follow great years which makes us optimistic about 2024. The economy is in reasonably good shape, inflation is moderating and corporate earnings projections are strong. That bodes well for future stock advances. There will be volatility and occasional pullbacks, but as long-term investors, we must trust that our diversified portfolios will fare well in any condition and will grow steadily over time.

Wishing you all a beautiful winter season and a prosperous New Year!

SCK