QUARTERLY
Market
REPORT

3RD QUARTER - 2023

High interest rates and stubborn inflation continued to stick around in the third quarter. But markets — and investors — have mostly shrugged off these challenges as the U.S. economy remains resilient.

RACING INTO THE SECOND HALF OF 2023

After an eventful second quarter featuring a mini banking crisis and debate around the debt ceiling, markets — and investors — welcomed the prospect of a potentially drama-free quarter. June's upward momentum carried over into July, which was a good month for markets despite another quarter-point interest rate hike from the Federal Reserve. The July increase took rates to their highest level in more than 22 years.[1]

Markets shrugged off the increase at first, choosing to focus instead on the possibility of the Fed pausing rate hikes in the latter months of 2023 and maybe even cutting rates in early 2024. But the optimism was somewhat short-lived as the July Consumer Price Index (CPI) report showed inflation ticking up to 3.2% instead of trending downward in response to the Fed's rate hikes.[2]

About the same time, Fitch Ratings downgraded U.S. debt in response to the debt-ceiling fallout earlier in the year. The price of gas also started to increase as foreign oil producers and threatening summer storms (including Hurricane Idalia on the Florida coast) once again snarled supply.

When inflation popped back up to 3.7% in August, it rattled the market's narrative that potential rate cuts may be on the horizon.[3] Concerns began to mount that the Fed would have to keep rates where they are and perhaps hike even further. In the end, the Fed chose not to hike rates at their September meeting but left the door open for additional hikes in the third quarter.

All these events dampened investors' enthusiasm, and equity markets ended mostly flat for the third quarter.

Equity Performance as of October 2, 2023					
Equity Index	Q3	YTD	1 YR	3 YRS	5YRS
S&P 500:	-3.65%	11.68%	19.59%	8.44%	8.03%
NASDAQ:	-4.12%	26.30%	25.00%	5.78%	10.44%
DJIA:	-2.62%	1.09%	16.65%	6.45%	4.84%

Source: Morningstar. Index Performance: Return (%). https://www.morningstar.com/indexes. Accessed October 2, 2023.

IT'S A MARATHON, NOT A SPRINT

So why isn't inflation coming down more quickly, despite the Fed's actions? For one, the economy has remained fairly (and somewhat surprisingly) robust. Gross domestic product (GDP) has accelerated over the past six months, growing by 2.2% in the first quarter and 2.1% in the second.[4]

Wage growth is a significant component of inflation, with employers paying more to hire and keep workers. Consumers are also spending, even as prices continue to increase.

In addition, higher interest rates don't impact energy prices, which remain elevated and volatile. Gas prices have been and continue to be a primary driver of inflation. Until energy costs smooth out, it likely will be difficult to drive inflation down to the target 2% without driving the U.S. into a recession.

HEADING INTO THE HOMESTRETCH

So far, 2023 has been fraught with challenges for investors — and new ones lie ahead, including a possible government shutdown, an autoworker strike and renewed worries about overly aggressive actions from the Fed. The 2024 election campaigns will also ramp up over the next few months, and markets may take a wait-and-see approach as candidates jockey for position on their party tickets.

But overall, it has been a good year for markets, even with these challenges. The jobs picture remains mostly strong, with the latest unemployment rate at 3.8%.[5] And as of mid-September, the Atlanta Fed was forecasting 4.9% GDP growth in the third quarter.[6] Though there will always be challenges to overcome, we are optimistic that markets will end 2023 strong.

Still, this is not a time to become complacent with your investments. We recommend reviewing your investments with your advisor and rebalancing your portfolio as needed to realign with your goals. As always, being deliberate and disciplined with your investing will typically yield the results that will align with your goals.

SOURCES
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[3] U.S. Bureau of Labor Statistics. Sept. 13, 2023. "Consumer Price Index – August 2023." https://www.bls.gov/news.release/pdf/cpi.pdf. Accessed Sept. 20, 2023.
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